In addition to turning the plain language of the statute on its head, the Seventh Circuit's decision also conflicts with the decisions of three other circuits and countless district courts that have interpreted SLUSA. As a result, the holdings of *Kircher II* and *Disher* combined eradicate a category of claims that have been traditionally left to state law, claims that were not Congress's focus when it enacted SLUSA and claims that, in fact, are not even so much as mentioned anywhere in SLUSA or its legislative history. The result of the Seventh Circuit's holdings is that shareholders like petitioner, who on the one hand have no federal remedy because their claims are not "in connection with" the purchase or sale of a security within the meaning of § 10(b), are now simultaneously denied a cause of action under state law because their claims *are* deemed to be "in connection with the purchase or sale" of a security within the meaning of SLUSA. According to the Seventh Circuit, Congress has stripped such investors – without ever bothering to mention them – of any direct private cause of action, concluding that their "'claims must be left to public enforcement.'" Pet. App. 10a (quoting *Kircher II*, 403 F.3d at 483-84).

OPINIONS BELOW

The district court's order granting plaintiff's motion to remand (Pet. App. 13a-14a) is unreported. The court of appeals' opinion finding appellate jurisdiction and reversing and remanding the district court's judgment with instructions to undo the remand order and to dismiss plaintiff's state-law claims (*id.* at 1a-11a) is reported at 419 F.3d 649.

JURISDICTION

The court of appeals entered its judgment on August 17, 2005. On November 9, 2005, Justice Stevens extended the time for filing a petition for a writ of certiorari to and including December 15, 2005. Pet. App. 75a. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

Relevant statutory and regulatory provisions are set forth at Pet. App. 50a-74a.

STATEMENT OF THE CASE

A. The Statutory Framework

In 1995, Congress passed the Private Securities Litigation Reform Act ("PSLRA") (codified in part at 15 U.S.C. §§ 77z-1, 78u) to prevent "strike suits," or meritless class actions alleging fraud in the securities market. *See* H.R. Conf. Rep. No. 105-803, at 13 (1998). To deter those suits, the PSLRA imposes stringent pleading and other procedural requirements on securities class-action plaintiffs. To avoid the PSLRA's requirements, plaintiffs increasingly brought suit against issuers in state court alleging securities fraud under state statutory or common law.

To prevent private plaintiffs from engaging in these alleged circumventions of the PSLRA, Congress passed SLUSA, which added to the Securities Act of 1933 ("1933 Act") and the Securities Exchange Act of 1934 ("1934 Act") identical provisions that preempt certain class actions under state law. SLUSA's preemption provision states:

> No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging –
>
> (1) an untrue statement or omission of a material fact in connection with the purchase or sale of a covered security; or
>
> (2) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.

15 U.S.C. § 77p(b); *accord id.* § 78bb(f)(1).[1] SLUSA also authorizes these actions to be removed to federal court:

> Any covered class action brought in any State court involving a covered security, as set forth in subsection (b) of this section, shall be removable to the Federal district court for the district in which the action is pending, and shall be subject to subsection (b).

Id. § 77p(c); *accord id.* § 78bb(f)(2). Under the Act, a "covered class action" includes a "lawsuit in which damages are sought on behalf of more than 50 persons or prospective class members," *id.* § 77p(f)(2)(A); *accord id.* § 78bb(f)(5)(B), and a "covered security" is a security that is either listed on a national securities exchange or issued by an investment company, *see id.* §§ 77p(f)(3), 77r(b)(1)-(2), 78bb(f)(5)(E).

B. Petitioners' Common-Law Claims

Petitioner is one of thousands of Citigroup customers who relied on Citigroup's investment reports and ratings in making the decision to continue holding certain stocks they already owned. Citigroup employs a five-point system to assess securities, rating securities as "buy," "outperform," "neutral," "underperform," or "sell" based on the current and anticipated performance of the security. Some time in 2000, Citigroup secretly ceased using its lowest two ratings – "underperform" or "sell" – for certain securities researched and rated by its Internet and Telecommunications Groups. Instead, it began rating those securities only as "buy," "outperform," or "neutral," even when the securities warranted a negative rating. Citigroup communicated to certain institutional customers

---

[1] The preemption provision quoted in the text comes from SLUSA's amendment to the 1933 Act. The preemption provision added by SLUSA to the 1934 Act, 15 U.S.C. § 78bb(f), is "functionally identical" to the 1933 Act amendment. *Kircher II*, 403 F.3d at 481. For ease of reference, the remainder of this brief refers only to the 1933 Act preemption provision.

that a rating of "neutral" indicated that they should sell the stock. Citigroup issued these misleading reports in an effort to secure additional investment banking business.[2]

In 1998 and 1999, petitioner acquired shares of MCI WorldCom Inc. and Rhythms Netconnections Inc. Relying on Citigroup's artificially inflated ratings of these stocks, petitioner retained these securities, which plummeted in value.

Petitioner filed a class action in Illinois state court, alleging that Citigroup breached its customer contracts and its fiduciary duty to its customers and acted negligently by failing to supervise its researchers and by issuing inaccurate, nonobjective investment reports, and that Citibank was unjustly enriched by not adequately performing services purchased by petitioner. *See* Pet. App. 25a-31a, 34a-37a (¶¶ 51-76, 83-94). Petitioner also alleged that Citigroup defrauded its customers by issuing misleading investment reports. *See id.* at 31a-33a (¶¶ 77-82). The complaint sought damages not to exceed $75,000 per class member.

Petitioner defined the class to include holders of the relevant securities – specifically, "all customers of [Citigroup] who held one or more of the Internet Stocks or Telecom Stocks in their [Citigroup] accounts at times when those stocks were declining in value and when [Citigroup] was rating those stocks as 'buy' 'outperform' or 'neutral' when such ratings were not warranted by [Citigroup's] research." *Id.* at 22a (¶ 39). The complaint explicitly excludes any claims based on Citigroup's "conduct in connection with [the] purchases or sales" of securities. *Id.* (¶ 41).

---

[2] *See, e.g.*, Conal Walsh, *Joe Public takes on giants of Wall Street*, The Observer (Apr. 14, 2002) (relating allegations that Jack Grubman, the "superstar" analyst for Salomon Smith Barney, issued misleading analyses of several companies in order to secure additional banking business), *at* http://observer.co.uk/business/story/0,,683827,00.html.

C. Proceedings Below

Citigroup removed to federal district court, arguing, *inter alia*, that the case fell within the district court's removal jurisdiction under SLUSA, *see* 15 U.S.C. § 77p(c), and that petitioner's claims were preempted by that Act, *see id.* § 77p(b). Petitioner moved to remand the case to state court for lack of subject-matter jurisdiction. The district court agreed with petitioner that it lacked jurisdiction.

The district court concluded that petitioner's common-law claims were outside the scope of SLUSA's removal provision because the claims were brought by holders of securities, not purchasers or sellers. *See* Pet. App. 39a-40a, 46a-47a. Because petitioner's claims were not "in connection with the purchase or sale of a covered security," the court explained, they were not cognizable under § 10(b) of the 1934 Act and therefore were not removable under SLUSA. The court accordingly remanded the case to state court for lack of subject-matter jurisdiction. *See id.* at 13a-14a.

The Seventh Circuit reversed and remanded with instructions to dismiss the case. The court first concluded that it had jurisdiction to review the district court's remand order, relying on its recent decision in *Kircher I*. *See id.* at 4a. In *Kircher I*, the Seventh Circuit acknowledged that, under 28 U.S.C. § 1447(d), a remand for lack of subject-matter jurisdiction is unappealable, but it held that a remand order under SLUSA is not based on a lack of subject-matter jurisdiction.

To reach that conclusion, the *Kircher I* court had opined that SLUSA permits removal of all "covered class actions" – that is, all class actions that seek damages on behalf of more than 50 investors, *see* 15 U.S.C. § 77p(f)(2)(A) – even though the Act preempts only "covered class actions" that meet the further requirement of alleging an untrue statement or omission, or use of a manipulative or deceptive device, "in connection with the purchase or sale of a covered security," *id.* § 77p(b). The court did not address

plaintiff's argument that the statutory language "as set forth in subsection (b)" makes clear that only those actions preempted by SLUSA are subject to removal. Rather, the court held that removal is proper even though a lawsuit is outside SLUSA's preemptive scope so long as the lawsuit is a "covered class action." The court thus reasoned that a SLUSA remand order of any class action involving more than 50 investors (*i.e.*, a "covered class action") is not one for lack of subject-matter jurisdiction. Such a remand order, the court then concluded, is one that may be reviewed on appeal.

The *Kircher I* court further explained that a remand under SLUSA is unlike a "[n]ormal" remand that "leave[s] all substantive issues open to plenary resolution in the state court," because whether SLUSA preempts a class action is "one specific substantive decision . . . [that] must be made by the federal rather than the state judiciary." 373 F.3d at 850. Under SLUSA, the court reasoned, state judges are incapable of making a preemption ruling, and thus "it is now or never for appellate review of the question whether an action under state law is preempted." *Id.*

Having determined that it could exercise appellate jurisdiction over the district court's remand order, the court in this case held that SLUSA preempted all of petitioner's state-law claims. The court observed that SLUSA was designed to prevent Rule 10b-5 private plaintiffs from migrating to state court to avoid the PSLRA. The court went on to note that, in *Blue Chip Stamps*, this Court had held that investors who neither purchase nor sell securities have no cause of action under § 10(b) and Rule 10b-5 as a result of those provisions' requirement that the unlawful conduct be "in connection with the purchase or sale" of securities. The court recognized that petitioner's complaint defined a class of non-trading shareholders who could not bring a private action under Rule 10b-5. *See* Pet. App. 6a, 10a-11a. The court nevertheless concluded that such non-traders' claims were "in connection with the purchase or sale" of securities and were thus preempted

by SLUSA, and that petitioner's complaint defined a class of non-trading shareholders who could not bring a private action under Rule 10b-5. *See id.* at 5a-6a, 9a, 10a. The court nevertheless concluded that petitioner's claims were "in connection with the purchase or sale" of securities and were preempted by SLUSA.

The court read *Blue Chip Stamps*' holding *not* as an interpretation of the "in connection with the purchase or sale" language in the 1934 Act, but rather as a mere policy-based, judicial limitation on the standing of private litigants to enforce § 10(b) and Rule 10b-5 that is not grounded in the text of § 10(b). *See id.* at 10a. The court concluded that, "'[b]y depicting their classes as containing entirely non-traders, plaintiffs do not take their claims outside § 10(b) and Rule 10b-5; instead, they demonstrate only that the claims must be left to public enforcement.'" *Id.* (quoting *Kircher II*, 403 F.3d at 483-84). In reaching that conclusion, the court acknowledged that its decision conflicted with decisions of the Second, Eighth, and Eleventh Circuits. *See id.* at 9a-10a.

REASONS FOR GRANTING THE PETITION

I. THE COURT SHOULD GRANT CERTIORARI TO REVIEW THE SEVENTH CIRCUIT'S HOLDING THAT REMAND ORDERS UNDER SLUSA ARE SUBJECT TO APPELLATE REVIEW

A. The Seventh Circuit's Exercise Of Appellate Jurisdiction Squarely Conflicts With Decisions Of Three Other Circuits

The Seventh Circuit's holding that it has jurisdiction to review a remand order based on a district court's finding that a plaintiff's claims are not preempted by SLUSA squarely conflicts with decisions of the Second, Ninth, and Eleventh Circuits. Those circuits hold that SLUSA's preemption and removal provisions are co-extensive – that is, that a state-law action that falls outside of SLUSA's preemptive scope is not removable under SLUSA. In their view, a district court's remand of such a lawsuit is based

on a lack of subject-matter jurisdiction and is not reviewable under § 1447(d).

By contrast, in *Kircher I*, the decision on which the court of appeals rested in this case, the Seventh Circuit insisted that SLUSA authorizes removal of class actions involving more than 50 investors and held that remands based on the conclusion that the claims are not preempted are not remands for lack of subject-matter jurisdiction. The division between the circuits is clear and stems from two opposing interpretations of SLUSA's removal provision: one (the Seventh Circuit's) that regards the provision as authorizing removal of all "covered class actions," and another (the Second, Ninth, and Eleventh Circuits') that regards it as authorizing removal only of those covered class actions described in SLUSA's preemption provision.

1. Second Circuit – *Spielman*

In *Spielman*, the Second Circuit addressed whether it could review a district court order granting a motion to remand after determining that the defendant's alleged misrepresentations were not "in connection with the purchase or sale" of securities, and that the plaintiff's claims were therefore not preempted by SLUSA. The Second Circuit stated that "SLUSA's removal provision makes removable any class action preempted by [SLUSA's preemption provision]." 332 F.3d at 123. In the Second Circuit's view, SLUSA completely preempts those class actions, but "only converts into federal claims those state claims that fall within its clear preemptive scope, thereby confining federal question jurisdiction under this statutory regime to a subset of securities fraud cases." *Id.* at 124.

The Second Circuit explained that, after a defendant removes an action under SLUSA, the district court must determine whether the action meets "the substantive requirements necessary to sustain removal under SLUSA's preemption provision": "If a district court determines the action is *not* a 'preempted class action' and, therefore, re-

moval was improper, the district court lacks subject matter jurisdiction to further entertain the action." *Id.* at 124-25. The Second Circuit concluded that, even though the district court in *Spielman* had not expressly stated that it was remanding for lack of jurisdiction, because the court had found the plaintiff's claims not to be preempted by SLUSA, its remand order was necessarily based on a lack of jurisdiction and consequently was not reviewable under § 1447(d).

The Second Circuit's decision squarely conflicts with *Kircher I* (and consequently the decision in this case), which held that a remand order that followed a finding of no preemption was not based on a lack of jurisdiction and *was* reviewable under § 1447(d). As Judge Newman succinctly explained in his *Spielman* concurrence, the issues "of complete preemption and the existence of subject matter jurisdiction ... are the opposite sides of the same coin." 332 F.3d at 132.

2. Ninth Circuit – *Abada*

In *Abada*, the Ninth Circuit reached a similar conclusion to that of the Second Circuit. The district court in *Abada* had found that the plaintiffs' claims were not preempted by SLUSA because they were not "in connection with the purchase or sale" of securities.

In accord with the Second Circuit, and in square conflict with the Seventh Circuit, the Ninth Circuit found that the district court's remand order was grounded on the absence of subject-matter jurisdiction and was not reviewable. Observing that SLUSA's removal provision "provides for the removal of 'any covered class action' 'based upon the statutory or common law of any State' 'alleging a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security,'" 300 F.3d at 1119 (quoting 15 U.S.C. § 78bb(f)(1) and (2)), the Ninth Circuit held that, "'[i]n order to decide whether it had subject matter jurisdiction, the district court was required to decide whether Abada's claims were completely preempted by SLUSA. Because construction of SLUSA was

necessary for the resolution of subject matter jurisdiction, [Ninth Circuit precedent] does not apply to create appellate jurisdiction." *Id.*; *see also United Investors*, *supra* (reaffirming the rule of *Abada*).

3. Eleventh Circuit – *Williams*

In *Williams*, decided after *Kircher I* but before the Seventh Circuit's decision in this case, the Eleventh Circuit addressed whether it could review a district court order remanding a lawsuit that had been removed under SLUSA, but that asserted claims only under federal law. The lawsuit in *Williams* was a "covered class action" involving a "covered security" as those terms are defined by SLUSA. 389 F.3d at 1186. But the district court remanded the case after it found that the lawsuit was not covered by SLUSA's preemption provision, because one of the requirements for preemption is that the action be "based upon the statutory or common law of any State or subdivision thereof," 15 U.S.C. § 77p(b). *See* 389 F.3d at 1188.

The Eleventh Circuit concluded that the remand was not reviewable under § 1447(d). It explained that, even though the district court never explicitly mentioned subject-matter jurisdiction, its remand order was based on a lack of removal jurisdiction. *See id.* at 1190 ("We therefore hold that the district court's remand order based on lack of removal jurisdiction, entered in response to a timely motion to remand, is not reviewable under § 1447(d).").[3] *Williams* thus squarely conflicts with the Seventh Circuit's position that a remand order based on a finding that a lawsuit is not preempted by SLUSA is reviewable.

---

[3] In *Riley*, the Eleventh Circuit had stated that, "in order to remove an action to federal court under SLUSA, the removing party must show that (1) the suit is a 'covered class action,' (2) the plaintiffs' claims are based on state law, (3) one or more 'covered securities' has been purchased or sold, and (4) the defendant misrepresented or omitted a material fact '*in connection with the purchase or sale of such security*.'" 292 F.3d at 1342.

A clear conflict exists, therefore, between the Seventh Circuit and the Second, Ninth, and Eleventh Circuits – and that conflict is openly acknowledged by the courts of appeals. *See Rowinski v. Salomon Smith Barney Inc.*, 398 F.3d 294, 298 n.2 (3d Cir. 2005) (noting "a division among the courts of appeals on an issue of appellate jurisdiction under SLUSA"). It is clear that the Seventh Circuit has no intention of rethinking its position in light of the views of the other circuits. *See* Pet. App. 4a ("declin[ing] to revisit" *Kircher I*). This Court's intervention therefore is necessary to establish the proper interpretation of SLUSA's removal provision and the reviewability of remand orders under SLUSA.

B. The Seventh Circuit's Exercise Of Appellate Jurisdiction Is Inconsistent With This Court's Precedents And The Language Of SLUSA

Not only does the Seventh Circuit's position conflict with the decisions of three other circuits, but it also is inconsistent with this Court's precedents. In *Things Remembered, Inc. v. Petrarca*, 516 U.S. 124 (1995), this Court stated that § 1447(d) bars appellate review of remands based on grounds recognized in § 1447(c), such as lack of subject-matter jurisdiction. *See id.* at 127-28. The Court held that this prohibition on appellate review extends not only to remand orders in suits removed under the general removal statute, but also to remand orders in cases removed under any other statute, even if the other statute contains an express remand provision of its own. *See id.* at 128. Moreover, this Court made clear in *Gravitt v. Southwestern Bell Telephone Co.*, 430 U.S. 723, 723 (1977) (per curiam), that it is immaterial whether the district court's decision that it lacked subject-matter jurisdiction was correct: § 1447(d) precludes review even of jurisdictional decisions that are clearly wrong.

The district court in this case interpreted SLUSA to authorize removal jurisdiction only over cases falling within SLUSA's preemption provision, and therefore remanded based on a perceived lack of subject-matter jurisdiction

once it determined that petitioner's claims were not preempted. *See, e.g.*, Pet. App. 46a-47a. Even if the district court was mistaken in its interpretation of SLUSA's removal provision – for example, because the Seventh Circuit is correct that SLUSA authorizes removal of all "covered class actions," not just preempted actions – the district court's order was still unreviewable under *Gravitt* and *Things Remembered*. The Seventh Circuit's exercise of appellate jurisdiction therefore conflicts with this Court's decisions.

In addition, the Seventh Circuit's interpretation of SLUSA's removal provision is incorrect and unsupported by the statutory text. As the Second, Ninth, and Eleventh Circuits noted, SLUSA's removal provision cross-references SLUSA's preemption provision. SLUSA does not permit removal of all covered class actions, but rather of "[a]ny covered class action brought in any State court involving a covered security, *as set forth in subsection (b)*," 15 U.S.C. § 77p(c) (emphasis added). Subsection (b) is the preemption provision. The plain language of the removal provision thus clearly indicates that Congress intended to authorize removal only of those "covered class actions" that also meet the requirements for preemption.

The Seventh Circuit's *Kircher I* opinion utterly failed to address that language or the conflicting circuits' interpretations of the removal provision. The Seventh Circuit simply chided the other circuits for being "mesmerized by the word 'jurisdiction,'" 373 F.3d 851, instead of recognizing that those courts quite naturally interpreted SLUSA to render removal proper only when an action is within the scope of § 77p(b). In addition, the Seventh Circuit's insistence (*id.* at 850) that *only* federal judges may resolve the issue of SLUSA preemption is an unprecedented reading of the statute, unsupported by text or legislative history, that conflicts with settled Supreme Court law regarding the ability of state courts to address a preemption defense. *See, e.g., Chick Kam Choo v. Exxon Corp.*, 486 U.S. 140, 149-50 (1988) ("[W]hen a state proceeding pre-

sents a federal issue, even a pre-emption issue, the proper course is to seek resolution of that issue by the state court.").

Finally, the Seventh Circuit in *Kircher I* advanced a red herring in stating that district courts lack subject-matter jurisdiction "only when Congress has not authorized the federal judiciary to resolve the sort of issue presented by the case," 373 F.3d at 849 (citing *Kontrick v. Ryan*, 540 U.S. 443, 452-56 (2004), and *Scarborough v. Principi*, 541 U.S. 401, 413-14 (2004)). The Seventh Circuit noted that § 77p(d)(4) provides that, "[i]n an action that has been removed from a State court pursuant to subsection (c) of this section, if the Federal court determines that the action may be maintained in State court pursuant to this subsection, the Federal court shall remand such action to such State court." 15 U.S.C. § 77p(d)(4). According to the Seventh Circuit, that subsection, coupled with SLUSA's removal provision, authorizes federal courts to determine whether an action is preempted by SLUSA. The court below thus reasoned that a remand after a finding of no preemption is not based on a lack of jurisdiction, because Congress has authorized the federal judiciary to resolve the issue of preemption. That reasoning misses the point by ignoring the statutory language fashioned by Congress. SLUSA specifically confers removal jurisdiction only on preempted actions. The fact that federal courts are "authorized" to resolve the issue of preemption in ruling on a motion to remand stems from the basic principle that federal courts have jurisdiction to determine their own jurisdiction. *See United States v. Ruiz*, 536 U.S. 622, 628 (2002).

Under SLUSA, after a defendant removes a case, a federal court must address the question of preemption to determine whether it has federal-question jurisdiction. A court's remand order based on a finding of no preemption is, for purposes of § 1447(d), no different from any other remand order based on a lack of federal-question jurisdiction following a defendant's removal of a case. The re-

moval in the instant case was initiated by respondent and was found improper by the district court. Nothing in *Kontrick* or *Scarborough* suggests that the district court's authority to resolve the preemption issue in ruling on motions to remand somehow meant that the court's remand order was not based on a lack of jurisdiction.

To the contrary, *Scarborough* explains that the "label" subject-matter jurisdiction refers to statutory prescriptions "'delineating the classes of cases . . . falling within a court's adjudicatory authority.'" 541 U.S. at 413-14 (quoting *Kontrick*, 540 U.S. at 454-55). By ignoring the crucial clause in § 77p(c) – "as set forth in subsection (b)" – the Seventh Circuit misunderstood that, under SLUSA, only that class of cases satisfying the requirements for preemption falls within a federal court's "adjudicatory authority" or removal jurisdiction. The Seventh Circuit thus incorrectly severed the jurisdictional issue from the substantive decision on preemption, when in fact the two "are the opposite sides of the same coin." *Spielman*, 332 F.3d at 132 (Newman, J., concurring).

C. The Reviewability Of Remand Orders Under SLUSA Is An Issue Of Great Importance Warranting This Court's Resolution

The circuit split over the reviewability of remand orders under SLUSA involves the core securities-litigation circuits and is unlikely to be resolved without this Court's intervention. The Seventh Circuit concluded in *Kircher I* that such orders were reviewable in full awareness that two circuits had held to the contrary, and there is no reason to think that the court will alter its view. *See* Pet. App. 4a ("declin[ing] to revisit" *Kircher I*). There is also no reason to think that the Second, Ninth, or Eleventh Circuits will reach a different conclusion regarding SLUSA remand orders based on the reasoning of the Seventh Circuit. Indeed, the Eleventh Circuit determined that such orders were not reviewable after the Seventh Circuit had decided the opposite in *Kircher I*.

Kircher I pointed out that the Second Circuit's decision in *Spielman* and the Ninth Circuit's decision in *Abada* predated *Scarborough* and *Kontrick*. *See* 373 F.3d at 850-51. But, as explained above, there is no reason to expect *Scarborough* or *Kontrick* to affect the analysis of the Second and Ninth Circuits. Moreover, as *Kircher I* recognized, *see id.*, the Ninth Circuit has reaffirmed the holding of *Abada* after *Kontrick*. *See United Investors*, *supra*.

The reviewability of remand orders under SLUSA is a question of great importance for the administration of the federal courts. That issue is central not just in cases involving "holder" claims, but in the entire range of cases in which plaintiffs successfully contest the applicability of SLUSA's preemption provision. Whether remand orders in such cases are subject to immediate appellate scrutiny has a significant impact not only on the dockets of the federal courts of appeals, but also on the ability of plaintiffs to obtain a timely adjudication of their viable state-law claims. Letting the Seventh Circuit's erroneous decision stand will undermine the "strong congressional policy against review of remand orders," *Things Remembered*, 516 U.S. at 136 (Ginsburg & Stevens, JJ., concurring) (internal quotation marks omitted), unfairly delaying legitimate state-court suits. *See Spielman*, 332 F.3d at 124. In his dissent in *Thermtron Products, Inc. v. Hermansdorfer*, 423 U.S. 336 (1976), then-Justice Rehnquist offered a cogent explanation of the reasons for precluding appellate review of remand orders:

> Congress' purpose in barring review of all remand orders has always been very clear – to prevent the additional delay which a removing party may achieve by seeking appellate reconsideration of an order of remand. The removal jurisdiction extended by Congress works a significant interference in the conduct of litigation commenced in state court. While Congress felt that making available a federal forum in appropriate instances justifies some such interruption and delay, it obviously thought it was

> equally important that when removal to a federal court is not warranted the case should be returned to the state court as expeditiously as possible. If this balanced concern is disregarded, federal removal provisions may become a device affording litigants a means of substantially delaying justice.

Id. at 354-55 (Rehnquist, J., dissenting).

This Court's intervention is warranted to prevent defendants from "substantially delaying justice" in class actions that SLUSA does not preempt and to resolve the disagreement among the courts of appeals over the reviewability of SLUSA remand orders.[4] Moreover, this case is a particularly suitable vehicle. Practically, this Court will have the opportunity to determine whether appellate jurisdiction exists over SLUSA remand orders only in a case

---

[4] The Class Action Fairness Act of 2005 ("CAFA"), which applies to class action suits commenced on or after February 18, 2005, does not diminish the importance of the jurisdictional question presented. CAFA establishes federal jurisdiction over certain class actions despite the absence of complete diversity of citizenship; permits removal of such actions; and authorizes appellate review of remand orders in such actions. *See* CAFA § 5(a), 119 Stat. 12 (to be codified at 28 U.S.C. § 1453(c)(1)) ("notwithstanding section 1447(d), a court of appeals may accept an appeal from an order of a district court granting or denying a motion to remand a class action to the State court from which it was removed"). CAFA's provisions do *not* apply to "any class action that solely involves . . . a claim . . . concerning a covered security as defined under section 16(f)(3) of the Securities Act of 1933 (15 U.S.C. 78p(f)(3)) and section 28(f)(5)(E) of the Securities Exchange Act of 1934 (15 U.S.C. 78bb(f)(5)(E))." *Id.* § 4(a)(2), 119 Stat. 11 (to be codified at 28 U.S.C. § 1332(d)(9)(A)); *accord id.* § 5(a), 119 Stat. 13 (to be codified at 28 U.S.C. § 1453(d)). CAFA thus specifically exempts securities class actions; SLUSA continues to govern such actions, and questions about the proper interpretation of SLUSA's preemption and removal provisions are no less important after passage of CAFA. In CAFA, Congress chose not to disturb the balance struck in SLUSA between federal and state prerogatives in securities litigation.

arising from a circuit that answers that question in the affirmative, and the only such circuit is the Seventh.[5]

The Court need not wait for a disposition of *Dabit*, in which the Court granted certiorari on September 27, 2005, before determining whether to grant certiorari in this case. *Dabit* does not involve the jurisdictional question presented here; the Court granted certiorari in *Dabit* to address whether SLUSA preempts claims brought by holders of securities. Moreover, the Court's decision on the merits in *Dabit* will not resolve the conflict in the circuits over whether SLUSA remand orders are reviewable. Whether SLUSA preempts holder claims is wholly independent of the question whether a district court's determination that a claim is not preempted, erroneous or not, is subject to immediate appellate review. *Disher* and *Kircher* are ideal companion cases to *Dabit*. Granting certiorari in those cases, as well as in *Dabit*, will ensure that the Court has the opportunity to resolve the procedural and the substantive confusion regarding the operation of SLUSA's preemption, removal, and remand provisions, 15 U.S.C. § 77p(b), (c), and (d)(4).

II. THIS COURT HAS GRANTED CERTIORARI IN *MERRILL LYNCH V. DABIT* TO DECIDE WHETHER SLUSA PREEMPTS CLAIMS BROUGHT BY HOLDERS OF SECURITIES

The division between the Seventh Circuit and the Second, Eighth, and Eleventh Circuits over whether SLUSA preempts holder claims reflects a deep confusion throughout the federal judiciary about SLUSA's preemptive scope. As one commentator has observed, "[t]he courts have struggled to interpret SLUSA's preemption provision, and the case law is in disarray." Jennifer O'Hare, *Preemption under the Securities Litigation Uniform Standards Act: If It Looks Like a Securities Fraud Claim and Acts Like a*

---

[5] On September 29, 2005, a petition for a writ of certiorari was filed in *Kircher* (No. 05-409). *Kircher* raises the same jurisdictional question as the one presented in this case.

Securities Fraud Claim, Is It a Securities Fraud Claim?, 56 Ala. L. Rev. 325, 326 (2004). This Court's intervention is required both to clarify the meaning of SLUSA's pre-emption provision and to ensure that holders of securities who have suffered damages from investment advisors' unlawful conduct are not deprived of their legitimate state-law claims.

A. The Seventh Circuit's Decision That SLUSA Preempts Holder Claims Squarely Conflicts With The Decisions Of Three Other Circuits

As the Seventh Circuit acknowledged in its opinion, its decision squarely conflicts with those of the Second, Eighth, and Eleventh Circuits. Those circuits have held that state-law claims in connection with the retention of securities fall outside of SLUSA's preemptive scope. The Seventh Circuit has gone even further because it has now eliminated claims where there were no purchases or sales by *anyone*, even though SLUSA's plain language preempts only claims "in connection with the purchase or sale of a covered security."

1. Second Circuit – *Dabit*

In *Dabit*, the Second Circuit held that the meaning of "in connection with" under SLUSA was "coterminous" with the meaning of the nearly identical language of § 10(b) and Rule 10b-5, and that the purchaser-seller rule of *Blue Chip Stamps* applies as a limit on SLUSA's "in connection with" requirement such that SLUSA does not preempt holding claims. 395 F.3d at 28. The Second Circuit began by observing that the phrase "in connection with the purchase or sale of a covered security" has been extensively interpreted by the Supreme Court and lower federal courts in the context of § 10(b) and Rule 10b-5 litigation. The Second Circuit explained that application of § 10(b) jurisprudence to SLUSA's language comports with the Act's stated goal of closing the "federal flight" loophole in the PSLRA:

> If the "in connection with" phrase is read to reach the same conduct under SLUSA as it does under § 10(b) and Rule 10b-5, then SLUSA will preempt precisely those state class actions which could be brought as federal actions subject to the heightened requirements of the PSLRA. If it were otherwise, actions might be preempted for meeting all of SLUSA's requirements, including the "in connection with" term, but not be capable of being brought under federal law for failure to meet the parallel requirement of Rule 10b-5, a result that the legislative history does not suggest Congress intended to produce in enacting SLUSA.

Id. at 36.

The Second Circuit rejected the precise argument endorsed by the Seventh Circuit: that the *Blue Chip Stamps* purchaser-seller rule is simply a judicially fashioned standing rule, not a textually based and substantive limit on the "in connection with the purchase or sale" language. The Second Circuit acknowledged that "[t]he limitation on standing to bring private suit for damages for fraud in connection with the purchase or sale of securities is unquestionably a distinct concept from the general statutory and regulatory prohibition on fraud in connection with the purchase or sale of securities." *Id.* at 39. But the court found that observation to have "little persuasive force in this context, because SLUSA deals with precisely the category of actions subject to the purchaser-seller rule":

> Once it is agreed that Congress deliberately borrowed SLUSA's "in connection with" language from § 10(b), the fact that the standing rule is analytically distinct from the underlying prohibition on fraud does not compel the conclusion that SLUSA preempts more than the purchaser/seller category of private damages claims over which the "in connection with" source language operates. Because *only* purchasers and sellers have a federal private damages remedy, it is far more natural to suppose that

> Congress meant to import the settled standing rule along with the "in connection with" phrase as a substantive standard. Nor are we moved by the observation that the standing rule is merely a judge-made gloss on the statute and the Rule, because private Rule 10b-5 damages actions are themselves a creature of judicial implication.

Id. at 39-40.

The Second Circuit concluded that SLUSA's "wholesale importation" of the language that gave rise to the "balancing judgment" of *Blue Chip Stamps* – namely, the judgment that "the judicially-adopted bar on federal non-purchaser and non-seller claims was counterbalanced by the existence of remedies under state law" – must "be presumed to represent a ratification of that judgment." *Id.* at 40. In sum, the Second Circuit anticipated, thoroughly analyzed, and squarely rejected the Seventh Circuit's reasoning regarding the applicability of SLUSA to holder claims.

2. Eighth Circuit – *Green*

Like the Second Circuit, the Eighth Circuit in *Green* turned to cases construing the identical language in § 10(b) and Rule 10b-5 to interpret the "in connection with the purchase or sale" language in SLUSA. The Eighth Circuit observed that, in *Blue Chip Stamps*, this Court refused to read that language broadly, limiting standing under § 10(b) and Rule 10b-5 to purchasers and sellers of securities. The Eighth Circuit concluded that "nonsellers and nonpurchasers of securities are not covered by SLUSA's preemption provision," because Congress enacted SLUSA in full awareness of the judicial gloss on § 10(b), "which acknowledged that causes of actions for the 'nonpurchase' or 'nonsale' of securities were not covered by the 1934 Act, and that state law would fill those gaps." 279 F.3d at 598 (internal quotation marks omitted). Like the Second Circuit's *Dabit* decision, the Eighth Circuit's decision squarely conflicts with the Seventh Circuit's decision in this case.

3. Eleventh Circuit – *Riley*

In *Riley*, the Eleventh Circuit concluded, based on the same analysis used by the Second and Eighth Circuits, that SLUSA does not preempt claims dealing with the retention of securities, rather than with purchase or sale. *See* 292 F.3d at 1345. The Eleventh Circuit stated that the "in connection with the purchase or sale" language of SLUSA is the same phrase in § 10(b) and Rule 10b-5, and it accordingly incorporates the judicial interpretations of that phrase. *See id.* at 1342-44. The Eleventh Circuit further noted that "[a]nalogizing to § 10b-5 is particularly appropriate because SLUSA was specifically enacted as an amendment to the 1933 and 1934 Acts." *Id.* at 1342.

As the Seventh Circuit acknowledged, its holding in this case that holder claims are preempted by SLUSA is in direct conflict with the decisions of the Second, Eighth, and Eleventh Circuits.

B. The Seventh Circuit's Interpretation Of SLUSA's Preemptive Scope Is Contrary To This Court's *Blue Chip Stamps* Decision And Congressional Intent

The Seventh Circuit's decision is also contrary to Supreme Court precedent. In *Blue Chip Stamps*, the Court interpreted § 10(b) and Rule 10b-5 to permit private lawsuits only by purchasers or sellers of securities. The Court made clear that the purchaser-seller rule, far from being untethered to the "in connection with the purchase or sale" language of § 10(b), was an interpretation of that language in the context of private securities litigation. For example, the Court stated that "the wording of § 10(b), making fraud *in connection with the purchase or sale of a security* a violation of the Act, is surely badly strained when construed to provide a cause of action, not to purchasers and sellers of securities, but to the world at large." 421 U.S. at 733 n.5.

Referring to *Birnbaum v. Newport Steel Corp.*, 193 F.2d 461 (2d Cir. 1952) – the Second Circuit opinion that origi-

nated the purchaser-seller rule – the Court observed that longstanding acceptance of "*Birnbaum's* reasonable interpretation of the wording of § 10(b), wording which is directed toward injury suffered 'in connection with the purchase or sale' of securities, argues significantly in favor of acceptance of the *Birnbaum* rule by this Court." 421 U.S. at 733 (footnote omitted). The Court added that "[t]he wording of § 10(b) directed at fraud 'in connection with the purchase or sale' of securities stands in contrast with the parallel antifraud provision of the 1933 Act," which reaches fraud "'in the offer or sale'" of securities, and that, "[w]hen Congress wished to provide a remedy to those who neither purchase nor sell securities, it had little trouble in doing so expressly." *Id.* at 733-34 (quoting 15 U.S.C. § 77q).

The Court's reliance on policy concerns in *Blue Chip Stamps* "to flesh out the portions of the law with respect to which neither the congressional enactment nor the administrative regulations offer conclusive guidance," *id.* at 737, does not mean that the purchaser-seller rule is not an interpretation of the "in connection with" phrase, albeit one guided by policy as well as text. SLUSA deals with private securities litigation and should be construed consistently with this Court's interpretation of the "in connection with the purchase or sale" language in such litigation. The Seventh Circuit was wrong simply to disregard *Blue Chip Stamps* after recognizing that the "in connection with" language of SLUSA is identical to and has the same scope as that in Rule 10b-5. *See* Pet. App. 9a-10a.

The Seventh Circuit's ruling also runs afoul of this Court's presumption against preemption. "'[B]ecause the States are independent sovereigns in our federal system, we have long presumed that Congress does not cavalierly pre-empt state-law causes of action.'" *Bates v. Dow Agro-Sciences LLC*, 125 S. Ct. 1788, 1807 (2005) (quoting *Medtronic, Inc. v. Lohr*, 518 U.S. 470, 485 (1996)). The presumption against preemption applies not only to the question whether Congress intended any preemption at all,

but also to questions about the scope of an express preemption statute. *See Medtronic*, *supra*.

As this Court recognized in *Blue Chip Stamps*, claims based on the retention of securities have traditionally been "available to nonpurchasers and nonsellers under state law." 421 U.S. at 739 n.9. Nothing in the text or background of SLUSA manifests a clear intent to preempt the state-law holding claims that *Blue Chip Stamps* acknowledged would be preserved. Indeed, the legislative history does not mention holding claims. *See Dabit*, 395 F.3d at 41-42 (discussing historical materials). SLUSA's language, the conference report recommending the bill, and the statements of SLUSA's proponents all indicate that the aim of SLUSA was to prevent circumvention of the PSLRA and therefore preempted only those claims that could be brought in federal court. *See id.* The Seventh Circuit's decision to the contrary is inconsistent with *Blue Chip Stamps*, as well as with this Court's preemption jurisprudence.

C. The Seventh Circuit Erred In Concluding That SLUSA Preempts Claims When There Has Been No Purchase Or Sale

The Seventh Circuit's implicit but unmistakable conclusion that SLUSA does not require an actual purchase or sale is remarkable given that the statute's explicit language requires the defendant's misconduct to be "in connection with *a purchase or sale*." Although in *Kircher II* the court went to great lengths to explain that the plaintiffs' market-timing claims included the claims of purchasers and sellers (while ignoring the fact that a market-timing injury is one that only a holder can sustain by definition), the court at least understood that SLUSA requires a purchase or sale. In *Disher*, however, all pretense is gone. The court itself recognized that the claim was brought on behalf of holders only. Citigroup therefore did not mislead or otherwise trick petitioner or any potential class member into purchasing or selling a stock. Rather, Citigroup misled petitioner and other holders into

retaining the stocks they already owned. This judicial revision of SLUSA thus goes well beyond even what the *Kircher II* court had done, and the conclusions of both courts are in square conflict with the decisions of every other circuit and numerous district courts to have addressed the issue.

D. Whether SLUSA Preempts Holder Claims Is An Issue Of Great Importance

As a result of Citigroup's misleading investment reports, thousands of investors have suffered substantial financial losses by retaining securities that have since bottomed out. In the Seventh Circuit's view, shareholders who have no federal remedy because their claims are not "in connection with the purchase or sale" of securities within the meaning of § 10(b) are now precluded by SLUSA from pursuing the traditional state-law remedies that have been open to them historically because their claims *are* "in connection with the purchase or sale" of securities within the meaning of SLUSA. But there is no mention anywhere in SLUSA or its legislative history of holder claims. "If Congress had intended to deprive injured parties of a long available form of compensation, it surely would have expressed that intent more clearly." *Bates*, 125 S. Ct. at 1801 (citing *Silkwood v. Kerr-McGee Corp.*, 464 U.S. 238, 251 (1984)). The Seventh Circuit's ruling leaves holders with *no* recourse – state or federal – against investment advisors who wrongfully induce them to retain poor investments.

Citigroup's misconduct is not unique. A number of investment advisors have been accused of issuing misleading research reports in an effort to secure additional investment banking business.[6] This Court's intervention is

---

[6] *See, e.g.*, Conal Walsh, *supra* note 2 (relating allegations that Henry Blodget, the "star analyst" for Merrill Lynch, issued misleading analyses of several companies in order to secure additional banking business); Rebecca Byrne, *Of Bubble Triumvirate, Only Meeker Remains*, TheStreet.com (Aug. 20, 2002) (noting allegations that Mary Meeker, one of Morgan Stanley's stock analysts, recommended "a plethora of

necessary to ensure that lawsuits arising from these events, involving numerous plaintiffs and billions of dollars in damages, are resolved correctly and consistently.

On September 27, 2005, this Court granted certiorari in *Dabit* to address whether, "as the Seventh Circuit held earlier this month and in direct conflict with the decision below, SLUSA preempts state law class action claims based upon allegedly fraudulent statements or omissions brought solely on behalf of persons who were induced thereby to hold or retain (and not purchase or sell) securities." Cert. Pet. at i, No. 04-1371. If the Court determines in *Dabit* that SLUSA does not preempt holder claims based upon allegedly fraudulent statements or omissions, its decision will very likely be dispositive of this case. On the other hand, if the Court concludes that SLUSA preempts such claims, that decision would not resolve the question whether SLUSA preempts Disher's claims that are not based upon allegedly fraudulent statements or omissions, such as his breach of contract and breach of fiduciary duty claims. If the Court does not grant this petition to address the jurisdictional question presented – which is not at issue in *Dabit* – it should hold the petition in this case pending resolution of *Dabit*, and then grant certiorari with respect to Question 2, if necessary.

---

questionable Internet stocks even as they fell to pennies a share" because her stock research was "biased" by "a desire to win banking business from those companies"), *at* http://www.thestreet.com/_tscs/markets/rebeccabyrne/10038386.html. *See also* SEC Litigation Release No. 18117 (Apr. 28, 2003), *at* http://sec.gov/litigation/litreleases/lr18117.htm (announcing details of SEC settlement with Morgan Stanley for the alleged provision of biased investment advice to clients); SEC Litigation Release No. 18116 (Apr. 28, 2003), *at* http://sec.gov/litigation/litreleases/lr18116.htm (same, for Lehman Brothers); SEC Litigation Release No. 18115 (Apr. 28, 2003), *at* http://sec.gov/litigation/litreleases/lr18115.htm (same, for Merrill Lynch and Henry Blodget).

CONCLUSION

The petition for a writ of certiorari should be held pending the resolution of *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit*, No. 04-1371, and the disposition of *Kircher v. Putnam Funds Trust*, No. 05-409, if the Court grants certiorari in *Kircher* before this petition is considered. In the alternative, the Court should grant the petition for a writ of certiorari.

Respectfully submitted,

ROBERT L. KING
701 Market Street
Suite 350
St. Louis, Missouri 63101
(314) 241-4844

DAVID C. FREDERICK
Counsel of Record
F. ANDREW HESSICK III
KELLOGG, HUBER, HANSEN, TODD, EVANS & FIGEL, P.L.L.C.
1615 M Street, N.W.
Suite 400
Washington, D.C. 20036
(202) 326-7900

December 15, 2005

Counsel for Petitioner

APPENDIX

TABLE OF CONTENTS

Page

Opinion of the United States Court of Appeals for the Seventh Circuit, *Disher v. Citigroup Global Markets Inc.*, No. 04-3073 (Aug. 17, 2005) 1a

Order of the United States District Court for the Southern District of Illinois, *Disher v. Citigroup Global Markets Inc.*, Civil No. 04-308-GPM (Oct. 25, 2005) 12a

Memorandum and Order of the United States District Court for the Southern District of Illinois, *Disher v. Citigroup Global Markets Inc.*, Civil No. 04-308-GPM (Aug. 10, 2004) 13a

Complaint, *Disher v. Citigroup Global Markets Inc.*, Civil No. 04-L-265 (3d Jud. Cir. Ct., Madison Cty., Ill. filed Mar. 22, 2004) 15a

Hearing Transcript for Motion To Remand, *Disher v. Citigroup Global Markets Inc.*, Civil No. 04-308-GPM (S.D. Ill. Aug. 9, 2004) (excerpt) 39a

Statutory and Regulatory Provisions Involved:

15 U.S.C. § 77p 50a
15 U.S.C. § 78j 55a
15 U.S.C. § 78bb 57a
28 U.S.C. § 1291 ..... 66a
28 U.S.C. § 1331 ..... 67a
28 U.S.C. § 1332 ..... 68a
28 U.S.C. § 1441 ..... 70a
28 U.S.C. § 1447 ..... 73a
17 C.F.R. § 240.10b-5 ..... 74a

Letter from Supreme Court Clerk regarding extension request for filing a petition for a writ of certiorari (Nov. 9, 2005) 75a

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

No. 04-3073

RICHARD DISHER, INDIVIDUALLY AND ON BEHALF OF ALL OTHERS SIMILARLY SITUATED,
Plaintiff-Appellee,

v.

CITIGROUP GLOBAL MARKETS INC.,
Defendant-Appellant.

Appeal from the United States District Court
for the Southern District of Illinois

[Argued Mar. 30, 2005]

[Decided Aug. 17, 2005]

Before BAUER, RIPPLE and KANNE, Circuit Judges.

RIPPLE, Circuit Judge.

On March 22, 2004, Richard Disher filed this action as a state-law putative class action against Citigroup Global Markets Incorporated, formerly known as Salomon Smith Barney ("SSB" or "Smith Barney"). SSB timely removed the case to the district court on the basis of federal question jurisdiction, *see* 28 U.S.C. § 1331; diversity of citizenship jurisdiction, *see id.* § 1332; jurisdiction related to bankruptcy proceedings, *see id.* § 1334(b); and preemption under the Securities Litigation Uniform Standards Act ("SLUSA"), *see* 15 U.S.C. § 78bb(f). On Mr. Disher's motion, the district court remanded the case to state court. For the reasons set forth in the following opinion, we now

reverse the judgment of the district court and remand the case for further proceedings.

I

BACKGROUND

A. State-Law Suit

Mr. Disher was a customer of SSB, which operated as a full-service securities firm. He purchased shares of MCI WorldCom Incorporated between April 16, 1998, and March 5, 1999. He also purchased shares of Rhythms Netconnections Inc. on August 11, 1999. As part of its services for its customers, SSB issued investment research reports and ratings on a stock's future performance. The subject of Mr. Disher's complaint included unspecified stocks researched and rated by SSB's Internet and Telecommunications research groups.

SSB represented that its reports employed a five-point rating system: "buy," "outperform," "neutral," "underperform" and "sell." R.2 at 3. Mr. Disher's complaint alleged that "no later than March 2000," SSB "secretly abandoned its published five-point rating system and instead utilized a *de facto* three-point system ('buy,' 'outperform,' and 'neutral')." *Id.* at 5. Specifically, a neutral recommendation allegedly was a coded message from SSB to certain institutional customers to sell a security. Also, instead of assigning an underperform or sell rating for a particular stock, SSB allegedly would stop covering that stock, with no public announcement or explanation. Thus, the complaint alleged, SSB's research ratings did not reflect its actual beliefs concerning the future performance of a stock.

The gravamen of the complaint was that SSB's misleading ratings induced Mr. Disher and class members to continue holding their securities in reliance on SSB's positive ratings when SSB's analysts no longer believed that such ratings were warranted. In addition, SSB also allegedly used its research reports, ratings and recommendations of certain stock to attract new, and to retain current, investment banking clients "by agreeing to issue a research rat-

ing for [those clients'] stock more favorably than Smith Barney's research warranted." *Id.* at 6.

Mr. Disher defined the putative class to include himself and "all customers of Smith Barney who held one or more of the Internet or Telecom Stocks in their Smith Barney accounts at times when those stocks were declining in value and when Smith Barney was rating those stocks as 'buy' 'outperform' or 'neutral' when such ratings were not warranted by Smith Barney's research." *Id.* at 8. The complaint specifically excluded "any claims based on Smith Barney's conduct in connection with Plaintiff's or any Class member's *purchases or sales* of any of the Internet Stocks or Telecom Stocks." *Id.* (emphasis added).

B. District Court Proceedings

SLUSA provides for the removal to federal court of certain class actions based on state law in which the plaintiffs allege "a misrepresentation or omission of a material fact *in connection with the purchase or sale* of a covered security." 15 U.S.C. § 78bb(f) (emphasis added). The district court ruled that SLUSA did not apply in this case because the alleged misconduct was not connected sufficiently to any purchase or sale of stock. Rather, the complaint alleged harm solely from the *retention* of securities in reliance on SSB's misleading research reports and ratings. The district court also concluded that there was no basis for removal under the general removal statute, 28 U.S.C. § 1441.

II
DISCUSSION

A. Standard of Review

A district court's decision regarding the propriety of removal is a question of federal jurisdiction that we review de novo. *Boyd v. Phoenix Funding Corp.*, 366 F.3d 524, 529 (7th Cir.2004). We also apply de novo review to the district court's interpretation of SLUSA. *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Lauer*, 49 F.3d 323, 326 (7th Cir.1995).

B. Removal and Preemption under SLUSA

On appeal, SSB challenges the district court's conclusion that Mr. Disher's action did not fall within SLUSA's preemptive scope.[1]

1.

As a threshold matter, Mr. Disher contends that we lack appellate jurisdiction over this matter because the district court remanded the case for lack of subject matter jurisdiction. *See* 28 U.S.C. § 1447(d). This court already has determined that a district court's remand of a case to state court based on SLUSA is appealable. *See Kircher v. Putnam Funds Trust* ("*Kircher I*"), 373 F.3d 847 (7th Cir. 2004). The substance of Mr. Disher's submissions in this case were addressed in *Kircher I*, and we decline to revisit this court's decision.

2.

SLUSA is the most recent in a line of federal securities statutes that originated with the enactment of the Securities Act of 1933 ("1933 Act"), 15 U.S.C. § 77a et seq., and the Securities Exchange Act of 1934 ("1934 Act"), 15 U.S.C. § 78a et seq. *See Riley v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 292 F.3d 1334, 1340 (11th Cir.), *cert. denied*, 537 U.S. 950, 123 S.Ct. 395, 154 L.Ed.2d 296 (2002). Section 10(b) of the 1934 Act made it "unlawful for any person . . . [t]o use or employ, *in connection with the purchase or sale of any security* registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the [Securities Exchange Commission ('SEC')] may prescribe." 15 U.S.C.

---

[1] Because, for the reasons we shall discuss in this opinion, we hold that Mr. Disher's cause of action is subject to removal and preemption under SLUSA, we have no occasion to address whether we have jurisdiction to review the district court's remand order, or to evaluate the merits of that order, with respect to the absence or presence of federal jurisdiction on any basis other than SLUSA.

§ 78j(2)(b) (emphasis added). The SEC then promulgated Rule 10b-5, which provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a mater.al fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, *in connection with the purchase or sale of any security*.

17 C.F.R. § 240.10b-5 (emphasis added). In 1995, Congress enacted the Private Securities Litigation Reform Act ("PSLRA"), 15 U.S.C. §§ 77z-1, 78u, to protect against merit-less shareholder suits that were being initiated for the sole purpose of obtaining large attorneys' fees through private settlements. *See Spielman v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 332 F.3d 116, 122 (2d Cir. 2003). To achieve this aim, the PSLRA imposed heightened pleading standards and mandatory stays of discovery for securities fraud class actions filed in federal court. *Id.*

After the enactment of the PSLRA, plaintiffs increasingly began to file suits in state courts under state securities law. *Id.* at 123. Congress responded by enacting SLUSA. *Kircher v. Putnam Funds Trust* ("*Kircher II*"), 403 F.3d 478, 482 (7th Cir.2005) ("SLUSA is designed to prevent plaintiffs from migrating to state court in order to evade rules for federal securities litigation in the [PSLRA]."). SLUSA attempts to close this "'federal flight' loophole" by making federal courts the exclusive forum for class actions alleging fraud in the sale or purchase of cov-

ered securities and by mandating that federal law governs such class actions. *Spielman*, 332 F.3d at 123. To that end, SLUSA contains the following preemption and removal provisions:

> (1) Class action limitations
>
> No covered class action[2] based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging –
>
> (A) a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security;[3] or

---

[2] SLUSA defines the term "covered class action" as

> (i) any single lawsuit in which –
>
> (I) damages are sought on behalf of more than 50 persons or prospective class members, and questions of law or fact common to those persons or members of the prospective class, without reference to issues of individualized reliance on an alleged misstatement or omission, predominate over any questions affecting only individual persons or members; or
>
> (II) one or more named parties seek to recover damages on a representative basis on behalf of themselves and other unnamed parties similarly situated, and questions of law or fact common to those persons or members of the prospective class predominate over any questions affecting only individual persons or members; or
>
> (ii) any group of lawsuits filed in or pending in the same court and involving common questions of law or fact, in which –
>
> (I) damages are sought on behalf of more than 50 persons; and
>
> (II) the lawsuits are joined, consolidated, or otherwise proceed as a single action for any purpose.

15 U.S.C. § 78bb(f)(5)(B).

[3] SLUSA defines the term "covered security" as

> a security that satisfies the standards for a covered security specified in paragraph (1) or (2) of section 18(b) of the Securities Act of 1933 [15 U.S.C. § 77r(b)], at the time during which it is alleged that the misrepresentation, omission, or manipulative or deceptive conduct occurred . . . .

15 U.S.C. § 78bb(f)(5)(E). Section 77r(b)(2), in turn, states:

(B) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.

(2) Removal of covered class actions

Any covered class action brought in any State court involving a covered security, as set forth in paragraph (1), shall be removable to the Federal district court for the district in which the action is pending, and shall be subject to paragraph (1).

15 U.S.C. § 78bb(f)(1)-(2).[4]

3.

A defendant may remove a case to federal court only if the federal district court would have original subject matter jurisdiction over the action. 28 U.S.C. § 1441; *Caterpillar Inc. v. Williams*, 482 U.S. 386, 392, 107 S.Ct. 2425, 96 L.Ed.2d 318 (1987). The party seeking removal has the burden of establishing federal jurisdiction. *Boyd*, 366 F.3d at 529. As a general rule, the plaintiff is the master of his own complaint and can avoid federal question jurisdiction by pleading exclusively state-law claims. *Bastien v. AT & T Wireless Servs., Inc.*, 205 F.3d 983, 986 (7th Cir. 2000) (citing *Franchise Tax Bd. v. Constr. Laborers Vacation Trust for S. Cal.*, 463 U.S. 1, 10, 103 S.Ct. 2841, 77 L.Ed.2d 420 (1983)). Ordinarily, when a claim arises under state law, the assertion of federal preemption as a defense will not create federal jurisdiction. *Id.*

"Congress has, however, created certain exceptions to" the well-pleaded complaint rule. *Beneficial Nat'l Bank v.*

A security is a covered security if such security is a security issued by an investment company that is registered, or that has filed a registration statement, under the Investment Company Act of 1940.

15 U.S.C. § 77r(b)(2).

[4] SLUSA amended both the 1933 Act, *see* 15 U.S.C. § 77p, and the 1934 Act, *see id.* § 78bb(f). The amendments are functionally identical; for ease of reference, we shall cite only the 1934 Act codification.

Anderson, 539 U.S. 1, 6, 123 S.Ct. 2058, 156 L.Ed.2d 1 (2003). The Supreme Court has declared that "a state claim may be removed to federal court in only two circumstances – when Congress expressly so provides . . . or when a federal statute wholly displaces the state-law cause of action through complete pre-emption." *Id.* at 8, 103 S.Ct. 2841. SLUSA expressly provides for the removal to federal court of covered fraud claims that are "in connection with the purchase or sale of a covered security." 15 U.S.C. § 78bb(f)(2).

SLUSA does not, however, preclude all securities fraud actions based on state law. To invoke SLUSA, the removing party must show: (1) that the action is a "covered class action" for purposes of SLUSA; (2) that the action purports to be based on state law; (3) that the defendant is alleged to have misrepresented or omitted a material fact (or to have employed a manipulative device or contrivance); and (4) that the defendant's alleged conduct was "in connection with the purchase or sale of a covered security." 15 U.S.C. § 78bb(f)(1)-(2); *Green v. Ameritrade, Inc.*, 279 F.3d 590, 596 (8th Cir.2002). The primary issue in this case concerns whether or not Mr. Disher's state-law class action complaint alleged misrepresentations that were "in connection with the purchase or sale" of securities. Mr. Disher contends that this action falls outside the scope of SLUSA because the complaint alleges that SSB's misrepresentations caused him and other class members to *hold* securities, not to purchase or sell them. Moreover, the complaint specifically disavows any claim related to the purchase or sale of stock.

SLUSA does not define "in connection with the purchase or sale of a covered security." The Supreme Court has not yet had occasion to consider this phrase in the context of SLUSA. For guidance, then, this court and other courts of appeals have relied on Supreme Court case law construing the identical phrase in the context of section 10(b) of the 1934 Act and Rule 10b-5. *See Kircher II*, 403 F.3d at 482-84 (collecting cases). The analogy to section 10(b) and

Rule 10b-5 is appropriate because, in enacting SLUSA, Congress "was using language that, at the time of SLUSA's enactment, had acquired settled, and widely-acknowledged, meaning in the field of securities law, through years of judicial construction in the context of § 10b-5 lawsuits." *Riley*, 292 F.3d at 1342-43. Analogizing to the case law interpreting section 10(b) also makes sense, in terms of our obligation to interpret the statute so as to give effect to the intent of Congress, because "SLUSA can do its job only if subsection (b) covers those claims that engage Rule 10b-5 (and thus come within the 1995 statute) if presented directly under federal law." *Kircher II*, 403 F.3d at 482.

The Supreme Court has limited the universe of investors who may bring private securities fraud actions under the statute. In *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 95 S.Ct. 1917, 44 L.Ed.2d 539 (1975), the Court held that investors who neither purchase nor sell securities have no standing to maintain private litigation to recover damages under section 10(b) and Rule 10b-5, even if the failure to purchase or sell was the result of fraud. Mr. Disher submits that, under *Blue Chip Stamps*, because claims related solely to the *retention* of securities, as opposed to a purchase or sale, are not cognizable under section 10(b), such claims also are not preempted by SLUSA. This position has the support of some of our sister courts of appeals. *See Dabit v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 395 F.3d 25, 43 (2d Cir.2005) ("[I]n enacting SLUSA Congress sought only to ensure that class actions brought by plaintiffs who satisfy the *Blue Chip* purchaser-seller rule are subject to the federal securities laws."); *Green*, 279 F.3d at 598; *Riley*, 292 F.3d at 1345.

However, this court recently has concluded that SLUSA's "in connection with the purchase or sale of a covered security" requirement does not incorporate the *Blue Chip Stamps* standing rule. *See Kircher II*, 403 F.3d at 483-84. Our opinion in *Kircher II* was issued after the district court's decision in this case and, indeed, after briefing

and oral arguments on appeal. In *Kircher II*, one of the plaintiffs' classes was defined as all investors who held the defendant mutual fund's securities during a defined period and did not purchase or sell shares during that period. *See id.* at 483. We held that the claims were "connected to their own purchase of securities" and thus were blocked by SLUSA. We explained:

> Decisions since *Blue Chip Stamps* reiterate that it deals with private actions alone and does not restrict coverage of the statute and regulation. *See United States v. O'Hagan*, 521 U.S. 642, 664, 117 S.Ct. 2199, 138 L.Ed.2d 724 (1997); *Holmes v. SIPC*, 503 U.S. 258, 284, 112 S.Ct. 1311, 117 L.Ed.2d 532 (1992); *United States v. Naftalin*, 441 U.S. 768, 774 n. 6, 99 S.Ct. 2077, 60 L.Ed.2d 624 (1979). By depicting their classes as containing entirely non-traders, plaintiffs do not take their claims outside § 10(b) and Rule 10b-5; instead they demonstrate only that the claims must be left to public enforcement. It would be more than a little strange if the Supreme Court's decision to block private litigation by non-traders became the opening by which that very litigation could be pursued under state law, despite the judgment of Congress (reflected in SLUSA) that securities class actions must proceed under federal securities law or not at all. *Blue Chip Stamps* combined with SLUSA may mean that claims of the sort plaintiffs want to pursue must be litigated as derivative actions or committed to public prosecutors, but this is not a good reason to undercut the statutory language.

Kircher II, 403 F.3d at 483-84. Mr. Disher's class definition of all SSB customers who *retained* certain securities in reliance on SSB's misrepresentations is no more narrowly drawn than the class definitions discussed in *Kircher II*. Thus, we must conclude that the present claims are connected sufficiently to the purchase and sale

of a covered security for the purposes of SLUSA preemption and removal.

Conclusion

Accordingly, we reverse the judgment of the district court and remand with instructions to vacate the remand order and to dismiss Mr. Disher's claims. SSB may recover its costs on this appeal.

REVERSED AND REMANDED

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF ILLINOIS

Civil No. 04-308-GPM

RICHARD DISHER, INDIVIDUALLY AND ON BEHALF OF ALL OTHERS SIMILARLY SITUATED,
Plaintiff,

v.

CITIGROUP GLOBAL MARKETS INC., D/B/A SMITH BARNEY,
Defendant.

[Filed Oct. 25, 2005]

ORDER

MURPHY, Chief District Judge:

On August 10, 2004, this Court remanded this action to state court for lack of subject matter jurisdiction. Defendant appealed that order, and the Seventh Circuit Court of Appeals held that this action was properly removed under the Securities Litigation Uniform Standards Act (SLUSA), 15 U.S.C. § 78bb(f), and SLUSA blocks Plaintiff's state law claims. *Disher v. Citigroup Global Mkts., Inc.*, 419 F.3d 649 (7th Cir. 2005). The Court of Appeals issued its opinion on August 17, 2005, and the mandate was entered on this Court's docket on September 13th.

In accordance with the Court of Appeals' mandate, this Court's August 10, 2004, order of remand (Doc. 36) is **VACATED**, and Plaintiff's claims are **DISMISSED with prejudice**. The Clerk of Court is **DIRECTED** to enter judgment accordingly.

IT IS SO ORDERED.

DATED: 10/25/05

/s/ G. PATRICK MURPHY
G. PATRICK MURPHY
Chief United States District Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF ILLINOIS

Civil No. 04-308-GPM

RICHARD DISHER, INDIVIDUALLY AND ON BEHALF OF ALL OTHERS SIMILARLY SITUATED,
Plaintiff,

v.

CITIGROUP GLOBAL MARKETS INC., D/B/A SMITH BARNEY,
Defendant.

[Filed Aug. 10, 2004]

MEMORANDUM AND ORDER

MURPHY, Chief District Judge:

Citigroup Global Markets, Inc. ("CGMI") removed this action on May 6, 2004, asserting federal subject matter jurisdiction on the basis of a federal question, diversity of citizenship, and bankruptcy. Insofar as those three theories of removal, for the reasons set forth on the record at the August 9, 2004, hearing, the Court lacks federal subject matter jurisdiction.

If that were the end of the issue, the Court would remand the action to state court pursuant to 28 U.S.C. § 1447(c). But in addition to the foregoing theories, CGMI also asserts that removal is proper by virtue of the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"). To establish that Disher's claims fall within SLUSA's preemptive scope, CGMI must show, among other things, that Disher alleges that CGMI engaged in fraudulent conduct "in connection with the purchase or sale of a covered security." 15 U.S.C. §§ 77p(b), 78bb(f)(1)(-2). *See also Green v. Ameritrade, Inc.*, 279 F.3d 590, 596 (8th Cir. 2002).

Removal was proper in the first instance as SLUSA contemplates that the district court is the proper judicial authority to determine whether this case is covered by the

statute. But the Court has determined, for the reasons set forth on the record, that this case does not involve misrepresentation or omissions of material fact "in connection with the purchase or sale of a covered security" as alleged by CGMI. Accordingly, insofar as SLUSA removal is concerned, the action is remanded to state court for further proceedings under state law.

Plaintiff's motion to remand is **GRANTED**, and this action is **REMANDED** to the Circuit Court for the Third Judicial Circuit, Madison County, Illinois. Defendant's oral motion for a stay is **DENIED**. The statute does not authorize the district court to issue a stay; it is only authorized to remand the case if the case does not fall under SLUSA preemptive scope.

IT IS SO ORDERED.

DATED: 8/9/04

/s/ G. PATRICK MURPHY
G. PATRICK MURPHY
Chief United States District Judge

IN THE CIRCUIT COURT
FOR THE THIRD JUDICIAL CIRCUIT
MADISON COUNTY, ILLINOIS

Cause No. 04-L-265

RICHARD DISHER, INDIVIDUALLY AND ON BEHALF OF ALL OTHERS SIMILARLY SITUATED,
Plaintiff,

v.

CITIGROUP GLOBAL MARKETS INC., D/B/A SMITH BARNEY,
Defendant.

[Filed Mar. 22, 2004]

COMPLAINT

NOW COMES Plaintiff Richard Disher, on his own behalf and on behalf of all others similarly situated, by and through his undersigned attorneys, and for his Complaint against Defendant Citigroup Global Markets, Inc., d/b/a Smith Barney, states:

THE PARTIES JURISDICTION AND VENUE

1. At all times relevant to this Complaint, Citigroup Global Markets Inc., and its predecessor firms, engaged in a full service securities business, including retail and institutional sales, investment banking services, trading, and it published company research reports, ratings and recommendations on stocks.

2. Citigroup Global Markets Inc., formerly known as Salomon Smith Barney, now does business as Smith Barney. Hereinafter throughout this Complaint, Citigroup Global Markets Inc. and its predecessor firms shall be re-

ferred to interchangeably as either "Citigroup Global Markets Inc." or "Smith Barney."

3. Smith Barney maintains offices throughout Illinois and specifically solicits business from residents of Madison County, Illinois.

4. Plaintiff Richard Disher is, and at all relevant times was, a resident of Alton, Illinois.

5. Plaintiff was at all relevant times a customer of Smith Barney or its predecessors in interest.

6. Plaintiff purchased shares of MCI Worldcom, Inc., between April 16, 1998, and March 5, 1999, and continued to hold those stocks during times relevant to this Complaint.

7. Plaintiff purchased shares of Rhythms Netconnections Inc., on August 11, 1999, and continued to hold those stocks during times relevant to this Complaint.

8. At times relevant to this Complaint, Plaintiff, as a customer of Smith Barney, received information concerning his account at his residence in Madison County through various means including telephone calls from Smith Barney's brokers and mailings in the form of monthly statements, confirmations and other correspondence. Venue is therefore proper in this Court.

GENERAL ALLEGATIONS

9. The volume and complexity of financial information and raw data which is available to investors – including, issuer disclosure statements, economic and employment statistics from governments, and marketing and purchasing trend reports from private sources – can often be overwhelming and confusing to investors. Research analysts play an important role in the relationship between companies and investors because of their expertise in assessing the available information.

10. During the relevant period Smith Barney engaged in a full-service securities business, including retail and institutional sales, investment banking services, trading and research. With respect to equity research, Smith

Barney divided its research analysts into groups that covered separate industry sectors. These groups published written research reports on selected companies with each sector.

11. Smith Barney provided its research as part of a package of services for its customers.

12. Each research report included an investment rating which Smith Barney used to make recommendations to its customers regarding the purchase and sale of stock in publicly traded companies.

13. During the relevant period, Smith Barney publicly represented that it used the following five-point rating system:

"1" Buy

"2" Outperform

"3" Neutral

"4" Underperform

"5" Sell

14. Smith Barney published its investment ratings knowing that the electronic and print media would report Smith Barney's rating to the investing public.

15. Smith Barney represented to the public and its customers that its analysts evaluated a company's "fundamentals," including its technology, products, services, financial performance, business plan, competition and other relevant information necessary to make a professional evaluation of a company's, and thus a stock's, future performance.

16. Smith Barney held out itself and its analysts as highly-skilled financial experts, possessing the special knowledge and expertise needed to analyze and evaluate a company's "fundamentals" and to predict the future performance of a company's stock.

17. Smith Barney represented such research reports, ratings and recommendations to reflect its analysts' objec-

tive and unbiased opinions regarding a stock's future performance.

18. Smith Barney intended for the investing public, and for its own customers in particular, to rely on Smith Barney's research, ratings and recommendations, as demonstrated by the fact that Smith Barney publicly touted the expertise of its research analysts, their research reports and Smith Barney's ratings and recommendations based on that research.

19. One group of Smith Barney research analysts (hereinafter referred to as the "Internet Group") researched certain Internet and similar technology companies and rated those companies' stocks (hereinafter referred to as the "Internet Stocks").

20. Another group of Smith Barney research analysts (hereinafter referred to as the "Telecommunications Group") researched telecommunications and similar technology companies and rated those companies' stocks (hereinafter referred to as the "Telecom Stocks").

21. The Internet Stocks and Telecom Stocks are the securities which are the subject of this Complaint. Plaintiff does not know all of the specific stocks research by the Internet and Telecommunications Groups, but such information is known to Smith Barney. However, the Rhythms Netconnections Inc. and the MCI Worldcom, Inc., stock Plaintiff held were among the stocks researched by the Telecommunications Group.

22. Smith Barney knew that when it issued "buy," "outperform" and "neutral" ratings for a stock (including Internet Stocks and Telecom Stocks), its customers were less likely to eliminate that stock from their investment portfolios, even in the face of adverse price movements of these securities.

23. Smith Barney knew that when it issued "sell" and "underperform" ratings for a stock (including Internet Stocks and Telecom Stocks), its customers were more

likely to eliminate that stock from their investment portfolios.

24. Thus, Smith Barney knew or should have known that investors its customers relied on its internet Group's and Telecommunications Group's research reports and specifically on their 5-point rating system.

25. At a time or times known more specifically to Smith Barney, but beginning no later than March 2000, Smith Barney began misusing its rating system and advance knowledge of the contents of its research reports, ratings and recommendations in various ways.

26. At a time known more specifically to Smith Barney, but beginning no later than March 2000, Smith Barney secretly abandoned its published five-point rating system and instead utilized a *de facto* three-point system ("buy," "outperform" and "neutral") for the Internet Stocks, although Smith Barney's published rating system continued to provide for "underperform" ("4") ratings "sell" ("5") ratings. Perhaps at the same time, but also during 2000 and at a time known more specifically to Smith Barney, Smith Barney secretly abandoned the five-point rating system in favor of the *de facto* three-point system for the Telecom Stocks as well.

27. Smith Barney's issuance of a "neutral" recommendation for an Internet or Telecom stock was a coded message to certain institutional customers to sell their securities.

28. In lieu of assigning "underperform" or "sell" recommendations for Internet Stocks and Telecom Stocks, Smith Barney instead quietly stopped covering the stock, without any announcement or meaningful explanation to the public or retail investors.

29. After discarding the five-point rating system in practice, neither the Internet Group nor the Telecommunications Group rarely again used a "4" ("underperform") and never used the "5" ("sell") rating for the Internet

Stocks or Telecom Stocks during the period relevant to this Complaint.

30. Thus, Smith Barney's research ratings for both the Internet Group and the Telecommunications Group did not actually reflect either a "1" out of five, or "2" out of five, or "3" out of five status.

31. As a result, Smith Barney's research ratings did not reflect Smith Barney's actual beliefs concerning the future performance of the Internet Stocks or Telecom Stocks.

32. One reason Smith Barney secretly abandoned the five-point rating system for the Internet Stocks and Telecom Stocks was so Smith Barney could continue to rate stocks as "buy," "outperform" or "neutral," even after Smith Barney's analysts no longer believed that such ratings were warranted for particular Internet Stocks and Telecom Stocks under the five-point rating system.

33. By continuing to rate the Internet Stocks and Telecom Stocks "buy," "outperform" or "neutral" under the secret three-point rating system, Smith Barney induced its customers to continue holding those securities, even after Smith Barney's analysts no longer believed that the "buy," "outperform" or "neutral" ratings were warranted.

34. Smith Barney also used the Internet Group's and Telecommunication Group's research reports, ratings and recommendations to attract new investment banking clients and to retain current investment banking clients by agreeing to issue a research rating for an investment banking client's stock more favorably than Smith Barney's research warranted.

35. Also, Smith Barney's Internet Group and Telecom Group research analysts were subjected to improper conflicts of interests because Smith Barney did not maintain proper separation between its research division and investment banking division.

36. Smith Barney allowed its investment banking division to exercise undue influence over the Internet

Group's and Telecommunications Group's analysts, including:

a. allowing the investment banking division to influence analysts' decisions regarding whether to provide research for a particular stock and how to rate that stock;

b. allowing the investment banking division to discourage the analysts from making statements or publishing research reports that could jeopardize existing or potential investment banking client relationships;

c. encouraging analysts to participate regularly in investment banking marketing activities prior to the publication of related research;

d. allowing investment banking clients to review draft research reports and ratings prior to publication; and/or

e. influencing analysts through a compensation system based in part upon analysts' contributions to investment banking revenue.

37. As a result of the undue influence of the investment banking division, the Internet Group and Telecommunications Group analysts:

a. refrained from issuing negative reports for companies with whom Smith Barney had, or was seeking, an investment banking relationship;

b. published research reports, ratings and recommendations more favorable than the research warranted; and/or

c. ceased issuing research altogether on such companies in order to avoid issuing a negative report.

38. Thus, contrary to Smith Barney's public representations that its research was independent and objective, the Internet Group and Telecommunications Group research was neither independent nor objective.

CLASS ALLEGATIONS

39. Plaintiff brings this class action against Smith Barney for himself individually and on behalf of all customers of Smith Barney who held one or more of the Internet Stocks or Telecom Stocks in their Smith Barney accounts at times when those stocks were declining in value and when Smith Barney was rating those stocks as "buy" "outperform" or "neutral" when such ratings were not warranted by Smith Barney's research, times which are known more specifically to Smith Barney.

40. Excluded from the Class are Smith Barney, and any parent, subsidiary, affiliate, or controlled person of Smith Barney, as well as any of their officers, directors, agents, servants or employees, and the immediate family members of any such person. Also excluded is any judge who may preside over this case and all persons who have claims in excess of $75,000.

41. Excluded from this Complaint are any claims based upon Smith Barney's conduct in connection with Plaintiff's or any Class member's purchases or sales of any of the Internet Stocks or Telecom Stocks.

42. In addition to the Rhythms Netconnections Inc. stock and MCI Worldcom, Inc. stock which Plaintiff owned, Plaintiff may also have held additional securities which are the subject of this Complaint. Whether Plaintiff in fact owned such additional securities cannot be ascertained by Plaintiff prior to discovery.

43. Plaintiff is a member of the Class and will fairly and adequately assert and protect the interests of the Class.

44. Plaintiff's interests are coincident with, and not antagonistic to, those of other members of the Class.

45. Plaintiff has retained attorneys who are experienced in class action litigation.

46. Members of the Class are so numerous and geographically dispersed that joinder of all Class members is impracticable. While the exact number and identity of

Class members cannot be ascertained by Plaintiff prior to discovery, Plaintiff believes that there are thousands of Class members and that their identity can be ascertained from Smith Barney's books and records.

47. There are questions of law or fact common to the Class, which common questions predominate over any questions affecting only individual members of the Class. Common questions include, but are not limited to, the following:

i. whether Smith Barney employed a *de facto* three-point rating system for the Internet Stocks and Telecom Stocks during the Class period;

ii. whether Smith Barney's *de facto* three-point rating system accurately reflected Smith Barney's analysts opinions regarding the Internet Stocks and Telecom Stocks;

iii. whether Smith Barney concealed its use of a *de facto* three-point rating system from Plaintiff and Class members;

iv. whether Smith Barney promised potential investment banking clients a "buy" or "outperform" rating in exchange for such investment banking business when the potential client's securities did not warrant a "buy" or "outperform" rating as determined under the five-point rating system;

v. whether Smith Barney promised not to downgrade existing investment banking clients' securities with a "underperform" or "sell" rating in exchange for such clients' continued business;

vi. whether Smith Barney gave Internet Stocks and Telecom Stocks more favorable ratings than were warranted as determined under the five-point rating system;

vii. whether Smith Barney's conduct which is the subject of this Complaint violated the constitution, rules, regulations, customs and usages of the New

York Stock Exchange rules or of the National Association of Securities Dealers;

viii. whether Smith Barney breached its contracts with Plaintiff and Class members;

ix. whether Smith Barney owed a fiduciary duty to Plaintiff and Class members;

x. whether Smith Barney violated its fiduciary duty to Plaintiff and Class members;

xi. whether as a result of its misconduct, Smith Barney was unjustly enriched at the expense of Plaintiff and Class members;

xii. whether Smith Barney's conduct which is the subject of this Complaint was negligent;

xiii. whether Smith Barney's conduct caused Plaintiff and Class members to sustain damages; and/or

xiv. the extent of any such damages.

48. The prosecution of separate actions by individual members of the Class would create a risk of:

a. inconsistent or varying adjudications with respect to individual members of the Class; and/or

b. adjudication with the respect to individual members of the Class, which would, as a practical matter, be dispositive of the interests of other members not parties to the adjudication or substantially impair or impede their ability to protest their interest.

49. The class action method is appropriate for the fair and efficient prosecution of this action.

50. Individual litigation of all claims, which might be brought by all Class members, would produce a multiplicity of cases so that the judicial system would be congested for years. Class treatment, by contrast, provides manageable judicial treatment calculated to bring a rapid conclusion to all litigation of all claims arising from the conduct of the Defendant.

COUNT I
(Breach of Contract)

51. Plaintiff realleges paragraphs 1 through 50 above, as though each were fully set forth in this Count.

52. Plaintiff and Class members became Smith Barney's customers by entering into contracts with Smith Barney.

53. Those standardized contracts provided in relevant part that "all transactions entered into under this Agreement shall be subject to any applicable constitution, rules, regulations, customs and usages of the exchange or market and its clearinghouse, if any, where such transactions are executed by you SBS or its agents your agents, subsidiaries and affiliates."

54. Thus, at all times relevant to this Complaint, transactions for Smith Barney's customers were subject to the rules of both the New York Stock Exchange ("NYSE") and the National Association of Securities Dealers ("NASD").

55. These contracts also provided in relevant part that "[t]his Agreement, all the terms herein, and all controversies described in Paragraph 6 shall be governed and construed in accordance with the laws of the State of New York . . . ." The controversies described in Paragraph 6 of the Agreement are

> all claims or controversies . . . between me and SBS [Smith Barney Shearson] and/or any of its present or former officers, directors, or employees concerning or arising from (I) any account maintained by me with SBS individually or jointly with others in any capacity; (II) any transaction involving SBS or any predecessor firms by merger, acquisition or other business combination and me, whether or not such transaction occurred in such account or accounts; or (III) the construction, performance or breach of this or any other agreement between us, any duty arising from the business of SBS or otherwise . . . .

56. NASD Conduct Rule 2110 requires members to observe high standards of commercial honor and just and equitable principles of trade.

57. NASD Conduct Rule 2210(d)(1)(A) states: "All member communications with the public shall be based on principles of fair dealing and good faith and should provide a sound basis for evaluating the facts in regard to any particular security or securities or type of security, industry discussed, or service offered. No material fact or qualification may be omitted if the omission, in the light of the context of the material presented, would cause the communications to be misleading."

58. NASD Conduct Rule 2210(d)(1)(B) prohibits members from making "[e]xaggerated, unwarranted or misleading statements or claims" in all public communications and states that "no member shall directly or indirectly, publish, circulate or distribute any public communication that the member knows or has reason to know contains any untrue statement of a material or is otherwise false or misleading."

59. NASD Conduct Rule 2210(d)(2)(C) prohibits members from making, "promises of specific results, exaggerated or unwarranted claims or unwarranted superlatives, opinions for which there is no reasonable basis or forecasts of future events which are unwarranted" in communications with the public.

60. NASD Conduct Rule 3010(a) requires members, to "establish and maintain a system to supervise the activities of each registered representative and associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with" NASD's own rules.

61. NYSE Rule 401 requires that member organizations adhere at all times to the principles of good business practice in the conduct of their business affairs.

62. NYSE Rule 476(a)(6) prohibits members from engaging in conduct or proceeding in a manner inconsistent with just and equitable principles of trade.

63. NYSE Rule 472 provides, that: "[n]o member or member organization shall utilize any communication which contains (i) any untrue statement or omission or a material fact or is otherwise false or misleading; or (ii) promises of specific results, exaggerated or unwarranted claims; or (iii) opinions for which there is no reasonable basis; or (iv) projections or forecasts of future events which are not clearly labeled as forecasts."

64. NYSE Rule 342(a) requires members, to maintain "appropriate supervisory control" over all business activities to ensure compliance with securities laws and regulations, including establishing "a separate system of follow-up and review to determine that the delegated authority and responsibility is properly exercised."

65. Smith Barney violated one or more of the foregoing NYSE and NASD rules, regulations, customs or usages by secretly abandoning the five-point rating system and secretly adopting the *de facto* three-point rating system as alleged above.

66. Smith Barney also violated one or more of the foregoing NYSE and NASD rules, regulations, customs or usages by permitting its investment banking division to unduly influence the Internet Group and Telecommunication Group analysts to issue or maintain non-objective research ratings for the Internet Stocks and the Telecom Stocks as alleged above.

67. By violating one or more of the NYSE and NASD rules, regulations, customs or usages, Smith Barney breached its contracts with Plaintiff and Class members.

68. Smith Barney's breaches of its contracts with Plaintiff and Class members were material.

69. As a direct and proximate result of Smith Barney's material breaches of its contracts with Plaintiff and Class members, Plaintiff and Class members have suf-

fered damages in an amount to be proven at trial but less than $75,000 per plaintiff or Class member.

WHEREFORE, Plaintiff requests that the Court certify an appropriate class in this case; enter judgment against Citigroup Global Markets Inc. and in favor of Plaintiff and the Class, with the total award not in excess of $75,000 per plaintiff or Class member; award to Plaintiff and the Class all damages resulting from Citigroup Global Markets Inc.'s unlawful conduct, and pre- and post-judgment interest and costs of suit; and grant such further relief as is appropriate under the circumstances.

COUNT II
(Breach of Fiduciary Duty)

70. Plaintiff realleges Paragraphs 1 through 50, 52 through 66 above, as though each were fully set forth in this Count.

71. At all times relevant to this Complaint, a special relationship of confidence, trust, or superior knowledge or control existed between Smith Barney and Plaintiff and each member of the Class as a result of the following:

a. Smith Barney encouraged Plaintiff and each member of the Class to place their utmost trust and confidence in Smith Barney's research report and its rating system;

b. Smith Barney assumed a position of trust and confidence by servicing and managing Plaintiff's and Class members' investments in Internet Stocks and Telecom Stocks;

c. Smith Barney held itself out to Plaintiff and Class members as a professional stock consultant firm, above and beyond its role as stock broker, advising Plaintiff and Class members which stocks they should buy or sell;

d. Smith Barney possessed exclusive control over its employees, including its Internet Group and Telecommunications Group analysts, and over their

compliance with NYSE and NASD rules, regulations, customs or usages;

e. Smith Barney possessed exclusive control over its research reports, ratings and recommendations;

f. Smith Barney possessed exclusive control over its use of its research reports, ratings and recommendations;

g. Smith Barney held out itself and its Internet Group and Telecommunications Group analysts as highly-skilled financial experts, possessing the special knowledge and expertise needed to analyze and evaluate a company's "fundamentals" and to predict the future performance era company's stock; and/or

h. Smith Barney is an investment firm characterized by elements of public interest which subject it to more stringent standards of conduct than those normally arising out of contract.

72. As a result of the foregoing, a fiduciary relationship existed between Smith Barney and Plaintiff and Class members.

73. Because of its fiduciary relationship, Smith Barney owed to Plaintiff and Class members a fiduciary duty which included:

a. a duty to act for or to give advice for the benefit of Plaintiff and each member of the Class with respect to matters within the scope of the relationship, which includes but is not limited to Smith Barney's research, ratings and recommendations with respect to the Internet Stocks and Telecom Stocks;

b. a duty to disclose all material facts to Plaintiff and each member of the Class with respect to matters within the scope of the relationship; and/or

c. a duty to adhere faithfully to the rules, regulations, customs and usages of the NYSE and NASD.

74. Smith Barney breached its fiduciary duty to Plaintiff and Class members in one or more of the following ways:

a. failing to disclose that one criterion Smith Barney used to select which Internet and Telecom Stocks it would research and rate was the existence of an investment banking or potential investment banking relationship with the company;

b. failing to disclose that the issuance of a "neutral" recommendation for an Internet or Telecom stock was a coded message to certain institutional customers to sell their securities;

c. failing to disclose the reason Smith Barney ceased researching and rating a previously covered Internet or Telecom Stock was to avoid the issuance of a negative research report, rating or recommendation for that company;

d. failing to disclose the improper influence it permitted its investment banking division to exercise over the Internet and Telecom Group analysts;

e. failing to disclose that its Internet and Telecom Group analysts were subject to the conflicts of interest alleged above;

f. failing to disclose that the 5-point rating system had become a *de facto* 3-point system designed to encourage Plaintiff and Class members to continue to hold the Internet and Telecom Stocks;

g. violating one or more of the foregoing NYSE and NASD rules, regulations, customs or usages by secretly abandoning the five-point rating system and secretly adopting the *de facto* three-point rating system as alleged above; and/or

h. violating one or more of the foregoing NYSE and NASD rules, regulations, customs or usages by permitting of its investment banking division to unduly influence the Internet Group and Telecommunication Group analysts to issue or maintain

non-objective research ratings for the Internet Stocks and the Telecom Stocks as alleged above.

75. Smith Barney wrongfully profited from its foregoing breaches of fiduciary duties to Plaintiff and Class members by collecting investment banking fees in return for not accurately rating the Internet Stocks and Telecom Stocks.

76. In addition, and as a direct and proximate result of Smith Barney's material breaches of fiduciary duty to Plaintiff and Class members, Plaintiff and Class members have suffered damages in an amount to be proven at trial but less than $75,000 per plaintiff or Class member.

WHEREFORE, Plaintiff requests that the Court certify an appropriate class in this case; enter judgment against Citigroup Global Markets Inc. and in favor of Plaintiff and the Class, with the total award not in excess of $75,000 per plaintiff or Class member; award to Plaintiff and the Class all damages resulting from Citigroup Global Markets Inc.'s unlawful conduct, and pre- and post-judgment interest and costs of suit, and punitive damages; require Citigroup Global Markets Inc. to disgorge all monies it obtained as a result of its unlawful conduct; and grant such further relief as is appropriate under the circumstances.

COUNT III
(Fraud)

77. Plaintiff realleges Paragraphs 1 through 50, 52 through 66 above, as though each were fully set forth in this Count.

78. As a result of Smith Barney's representations to Plaintiff and Class members as alleged above, Smith Barney assumed a duty to disclose to Plaintiff and Class members:

a. material changes in Smith Barney's evaluations, recommendations and ratings of the Internet Stocks and Telecom Stocks with respect to which it had previously issued reports, recommendations and ratings; and/or

b. material changes in Smith Barney's research, recommendation and ratings practices.

79. Smith Barney made one or more of the following false and fraudulent representations to Plaintiff and Class members:

a. Smith Barney used a five-point rating system for rating Internet Stocks and Telecom Stocks;

b. Smith Barney's ratings of certain of the Internet Stocks and Telecom Stocks were based upon its analysts' objective evaluations of the concerned company's "fundamentals," including its technology, products, services, financial performance, business plan, competition and other relevant information necessary to make a professional evaluation of a company's and thus a stock's future performance; and/or

c. Smith Barney's ratings of certain Internet Stocks and Telecom Stocks warranted a "buy," "outperform" or "neutral" rating when, in fact, Smith Barney's internal research and evaluation of those companies warranted a "underperform" or "sell" rating.

80. Smith Barney also fraudulently concealed from Plaintiff and Class members one or more of the following facts:

a. Smith Barney used a *de facto* three-point rating system for rating Internet Stocks and Telecom Stocks;

b. Smith Barney's ratings of certain of the Interact Stocks and Telecom Stocks were issued to attract or maintain certain investment banking clients and were not based upon Smith Barney's analysts' objective evaluations of the concerned company's "fundamentals," including its technology, products, services, financial performance, business plan, competition and other relevant information neces-

sary to make a professional evaluation of a company's and thus a stock's future performance;

c. Smith Barney's Internet Group and Telecommunications Group analysts were compensated based in part upon the success of Smith Barney's investment banking division, and the analysts' compensation was directly correlated to the analysts' favorable research reports, ratings and recommendations for Smith Barney's existing or prospective investment banking clients;

d. All or more than a *de minimis* portion of Smith Barney's investment banking business involving the Internet Stocks and Telecommunications Stocks was dependent on Smith Barney's issuance of favorable research reports, ratings and recommendations for those securities;

e. The Internet Group's and Telecom Group's analysts were issuing their reports, ratings and recommendations despite their conflicts of interest as alleged above, and these conflicts of interest materially influenced Smith Barney's research reports, ratings or recommendations of certain Internet Stocks and Telecom Stocks; and/or

f. The research reports, ratings and recommendations of the Internet Group and the Telecommunications Group did not accurately reflect those analysts' true opinions of certain Internet Stocks and Telecommunications Stocks.

81. The foregoing misrepresentations were material, and the foregoing facts which Smith Barney concealed were material.

82. As a direct and proximate result of Smith Barney's fraud as alleged above, Plaintiff and Class members have suffered damages in an amount to be proven at trial but less than $75,000 per plaintiff or Class member.

WHEREFORE, Plaintiff requests that the Court certify an appropriate class in this case; enter judgment against

Citigroup Global Markets Inc. and in favor of Plaintiff and the Class, with the total award not in excess of $75,000 per plaintiff or Class member; award to Plaintiff and the Class all damages resulting from Citigroup Global Markets Inc.'s unlawful conduct, pre- and post-judgment interest and costs of suit, and punitive damages; require Citigroup Global Markets Inc. to disgorge all monies it obtained as a result of its unlawful conduct; and grant such further relief as is appropriate under the circumstances.

COUNT IV
(Unjust Enrichment)

83. Plaintiff realleges Paragraphs 1 through 50 above, as though each were fully set forth in this Count.

84. Smith Barney was at all relevant times a member of the NYSE and NASD.

85. Plaintiff realleges Paragraphs 54 and 56 through 66 above, as though each were fully set forth in this Count.

86. As a direct and proximate result of Smith Barney's foregoing acts and omissions, Smith Barney was enriched at the expense of Plaintiff and the Class by collecting investment banking fees in return for not accurately rating the Internet Stocks and Telecom Stocks.

87. Smith Barney's retention of the benefits it received would be unjust such that equity and good conscience require that Smith Barney be required to disgorge the benefits it has unjustly received.

WHEREFORE, Plaintiff requests that the Court certify an appropriate class in this case; enter judgment against Citigroup Global Markets Inc. and in favor of Plaintiff and the Class, with the total award not in excess of $75,000 per plaintiff or Class member; require Citigroup Global Markets Inc. to disgorge all monies it obtained as a result of its unlawful conduct, and pre- and post-judgment interest and costs of suit; and grant such further relief as is appropriate under the circumstances.

COUNT V
(Negligence)

88. Plaintiff realleges Paragraphs 1 through 50 above, as though each were fully set forth in this Count.

89. Smith Barney was at all relevant times a member of the NYSE and NASD.

90. Plaintiff realleges Paragraphs 54 and 56 through 66 above, as though each were fully set forth in this Count.

91. Smith Barney held itself out as a skilled specialist in the field of investment research, possessing the specialized knowledge, skill and care ordinarily used by reasonably well-qualified members of the investment research and consultant professions.

92. It thereby became Smith Barney's duty to exercise that degree of knowledge, skill and care ordinarily used, or which should be used, by reasonably well-qualified members of the investment research profession, including but not limited to the duties:

a. to issue research reports, ratings and recommendations that accurately reflect the independent and objective opinions of its research analysts;

b. to establish and enforce adequate policies and procedures to maintain the independence of its research analysts;

c. to establish and enforce adequate policies and procedures to prevent conflicts of interests of its research analysts;

d. to disclose any conflicts of interests of its research analysts;

e. to establish and enforce adequate policies and procedures to ensure that its research reports, ratings and recommendations were not influenced by existing or potential investment banking client relationships;

f. to adhere to the rules, regulations, customs and usages of the NYSE and NASD;

g. to use the rating system it represented it was using; and/or

h. to advise its customers of any material changes in its rating system.

93. Smith Barney was negligent in one or more of the following ways:

a. failing to establish and enforce adequate policies and procedures to maintain the independence of research analysts in of the Internet Group and the Telecommunications Group from Smith Barney's investment banking function sufficient to ensure objective and uncompromised research;

b. permitting its Internet Group and Telecommunications Group research analysts to be unduly influenced by and subjected to conflicts of interest from the investment banking function of Smith Barney;

c. failing to establish and enforce adequate policies and procedures to ensure objective and uncompromised research of its Internet Group and Telecommunications Group research analysts;

d. failing to establish and enforce adequate policies and procedures to ensure Smith Barney's adherence to NYSE and NASD rules, regulations, customs or usages;

e. failing to adhere to NYSE and NASD rules, regulations, customs or usages;

f. issuing research reports, ratings and recommendations that did not accurately reflect the independent and objective opinions of its research analysts;

g. failing to disclose its Internet Group and Telecommunications Group analysts' conflicts of interest as alleged above;

h. failing to adhere to the rules, regulations, customs and usages of the NYSE and NASD;

i. failing to use the 5-point rating system it represented it was using; and/or

j. failing to advise its customers of the abandonment of the 5-point rating system in favor of the *de facto* 3-point system.

94. As a result of Smith Barney's foregoing negligence, Plaintiff and Class members have suffered damages in an amount to be proven at trial but less than $75,000 per plaintiff or Class member.

WHEREFORE, Plaintiff requests that the Court certify an appropriate class in this ease; enter judgment against Citigroup Global Markets Inc. and in favor of Plaintiff and the Class, with the total award not in excess of $75,000 per plaintiff or Class member; award to Plaintiff and the Class all damages resulting from Citigroup Global Markets Inc.'s unlawful conduct, and pre- and post-judgment interest and costs of suit; and grant such further relief as is appropriate under the circumstances.

KOREIN TILLERY

/s/ Stephen M. Tillery
STEPHEN M. TILLERY #2834995
701 Market Street, Suite 300
St. Louis, Missouri 63101
Voice: (314) 241-4844
Fax: (314) 241-35251854

SWEDLOW & KING LLC
STEPHEN A. SWEDLOW #6234550
ROBERT L. KING #6209033
Three First National Plaza
70 West Madison Street, Suite 660
Chicago, Illinois 60602
Voice: (312) 899-5063
Fax: (312) 641-9555

THE SIMMONS FIRM LLC
ROSALIND M. ROBERTSON, #6278330
DEREK Y. BRANDT, #6228895
CHRISTOPHER N. MESSINA, #6243490
JEFFREY S. COOPER, #6229060
707 Berkshire Blvd.
East Alton, IL 62024
Voice: (618) 259-2222
Fax: (618) 259-2251

ATTORNEYS FOR PLAINTIFF

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF ILLINOIS

Civil No. 04-308-GPM

FICHARD DISHER, INDIVIDUALLY AND ON BEHALF OF ALL OTHERS SIMILARLY SITUATED,
Plaintiff,

v.

CITIGROUP GLOBAL MARKETS INC., D/B/A SMITH BARNEY,
Defendant.

[Aug. 9, 2004]

MOTION TO REMAND

* * * * *

[3] COURTROOM DEPUTY: *Richard Disher versus Citigroup Global Markets, Inc*, Case No. 03-308-GPM, motion to remand. Will the parties please identify themselves for the record.

MR. TILLERY: For the plaintiff, your Honor, it is Steve Tillery and Steve Barash.

THE COURT: Mr. Tillery.

MS. HUANG: Joyce Huang.

MR. WHYTE: Joe Whyte with Heyl, Royster.

* * * * *

[18]

* * * * *

THE COURT: It seems to me the rest of these – I understand your arguments. I don't marginalize them. I just don't think they make it. But I'm interested in your SLRA argument.

MS. HUANG: I think the crux of this SLUSA issue is that in this case the key fact is the investment decisions that

are the subject of this action. Plaintiffs' decision to hold these stocks –

THE COURT: Right.

MS. HUANG: – were made in connection with CGMI brokage [*sic*] accounts, every single one of them. The putative class is defined as those persons who have brokerage accounts at CGMI and it is in connection with their reliance on CGMI research reports that they obtained –

THE COURT: They held them.

MS. HUANG: But they obtained because they had these accounts, but they held them based on those research reports. And it was based on those research reports that they made those investment decisions in their accounts.

The relevant authority is the SEC brief. The SEC has taken the position in the briefs submitted in *Gray* and *Dabit*, which were submitted to this court for consideration, that in [19] those circumstances where the investment decisions were taken in connection with a brokage [*sic*] account the whole purpose of which is to purchase and sell securities. In those circumstances those investment decisions satisfied the in-connection-with-a-purchase-or-sale requirement of SLUSA. And the SEC has a very important institutional enforcement issue at stake which is why it is trying to enforce and set forth its position on this matter. Which is, the SEC points out very clearly in the *Dabit* amicus brief that was submitted to the court that there are actually two components to the in-connection-with-a-purchase-of-sale of a security in a 10(b) case. In a 10(b) case there is a requirement that any –

THE COURT: But this is not a 10(b) case.

MS. HUANG: It is not a 10(b) case. But all the parties agree and the cases all agree that the question of how to interpret that language in SLUSA is that you should interpret it exactly as it is interpreted in 10(b). And so in 10(b) there is two components which I think that plaintiff has conflated that are separate. There is a requirement of Section 10(b) that any misrepresenting be made in connec-

tion with the purchase or sale of a securities that is a very flexible requirement. There is the separate requirement of standing under the *Blue Chip Stamps* case that says in order for a plaintiff to have standing to assert a 10(b) case in a private right of action that plaintiff actually must have [20] purchased or sold the securities.

THE COURT: Right.

MS. HUANG: That is a different and separate requirement from the 10(b) requirement of in connection with a purchase or sale. In fact, and the reason this is important is, as the SEC points out, when the SEC brings a 10(b) case the SEC does not have to comply with the *Blue Chips Stamp* requirement that the SEC has purchased or saled [*sic*] or show that anybody purchased or saled [*sic*].

THE COURT: It has statutory standing is the magic word.

MS. HUANG: Correct. And all the SEC has to prove is what 10(b) requires, which is in connection with the purchase or sale of securities. Because of the in-connection language the courts have interpreted that language only to require that the person making the statement have done so with a – in a way that was reasonably calculated to influence the investing public. There is no requirement in 10(b) itself that any actual person have purchased or sold the security at issue. It is only the *Blue Chips Stamp* standing requirement that implements that requirement.

And again the reason the SEC thinks this is important is the SEC says if you begin to interpret the in-connection-with-purchase-or-sale-of-securities language in 10(b) as itself requiring that persons have purchased or sold [21] the securated [*sic*] issue then the SEC will be hampered in its enforcement efforts because that requirement will apply to the private – to the actions that the SEC brings on enforcements behalf.

THE COURT: Let me stop you there.

MS. HUANG: Of course.

THE COURT: Of course when the SEC brings a 10(b) action we don't have to worry about jurisdiction, do we? The case may be good or the case may be bad, but the court's subject matter jurisdiction is a given.

MS. HUANG: That's correct. But the issue here is not the question of whether there is subject matter jurisdiction in those cases, but how to interpret the language in-connection-with-the-purchase-or-sale.

THE COURT: Well, yes. But see, as I see it in that case we're talking about the statutory construction to be placed on what is admittedly a remedial statute and the extent of it. Now here we're talking about the court's subject matter jurisdiction and all the intendments and presumptions run against your argument, not for it. In other words, here it is a narrow construction that the district court is never to expand jurisdiction. Isn't that the distinction here?

MS. HUANG: I don't think there is an expansion of jurisdiction. In fact, if we can get down to brass tacks. I think what plaintiffs' are alleging is we have a holder claim. [22] Holder claims are not cognizable under 10(b).

THE COURT: Exactly.

MS. HUANG: However, what the Supreme Court says in the *Dabit* brief, and this is the argument the SEC making in these analysis cases that are being brought across the country, the – with respect to the purchase or sale requirement. In *Blue Chip Stamps* the court recognized that holders – a holder claim is a violation of 10(b). In *Blue Chip Stamps* the United States Supreme Court says: A person who decides to hold a security based on a misrepresentation is someone who is experiencing a violation of 10(b).

THE COURT: Right.

MS. HUANG: The court said in *Blue Chips* we are not going to allow that holder to sue under 10(b). We're going to implement a standing requirement which is separate from the in-connection-with-a-purchase-or-sale requirement because these holder claims are too hard to prove. It's just

too hard to prove that someone held rather than purchased or sold and we are going to sacrifice those claims in order to have clarity in 10(b).

So in other words, what the Supreme Court – what the SEC says in the *Dabit* brief says: The Supreme Court has recognized that under 10(b) the requirement of in connection with a purchase of [*sic*] sale of securities is satisfied where someone holds in reliance on alleged misrepresentation. It is [23] just that the Supreme Court had a separate standing requirement in *Blue Chip Stamps* that is different from the in connection with purchase or sale.

THE COURT: How does that help you here?

MS. HUANG: That helps me here is because what the SEC is saying is here in SLUSA we are only talking about the in-connection-with-a-purchase-or-sale requirement. There is no need and it would be inappropriate to import into SLUSA the *Blue Chips Stamp* separate holding – the separate standard requirement that the person actually have purchased or sold. What the SEC says in the *Dabit* amicus brief is where a holder says that they held in connection with decisions with alleged misrepresentations that holding is in connection with a purchase or sale of a security. Now it is true that that holding doesn't satisfy the *Blue Chips* standard requirement but that's not a requirement –

THE COURT: What you are saying is, though, you like the argument that the SEC is making.

MS. HUANG: Yes.

THE COURT: But, I mean, that's just what it is. It is just an argument. It's whether the court would be more impressed with the SEC's argument than it would be with Mr. Whyte's argument is at best –

MS. HUANG: Well, two things. First, I think the SEC's position on this issue is entitled to deference because [24] this is a decision the SEC is making in furtherance of its ability to enforce.

THE COURT: You think the *Chevron* standard applies in this case?

MS. HUANG: Not the *Chevron* standard but the SEC is entitled to – what it is trying to do –

THE COURT: What other kind of deference is there?

MS. HUANG: I think what's important is when the court – because, as you know, under the *Kircher* case these decisions all will now be appealed immediately.

THE COURT: Right.

MS. HUANG: The crucial issue that the SEC is going around to these circuit courts and submitting this amicus brief the reason the SEC thinks it is a crucial issue and thinks it is important for the courts of appeals to come out the right way is, if there's a different interpretation of in-connection-with-a-purchase-or-sale the SEC will be hampered in its ability to enforce these cases. The SEC will there – this importation of the standard requirement of *Blue Chip Stamps* into the in-connection-with-the-purchase-or-sale-of-securities language in the 10(b), the SEC says in the *Dabit* brief, will require it to meet a higher standard any time it wants to shows a 10(b) violation.

THE COURT: I see what you are saying. They're [25] worried how it would affect –

MS. HUANG: The interpretation of 10(b). Because SLUSA and 10(b) –

THE COURT: But you are not making the argument that this is an administrative decision entitled to deference under *Chevron*. You are saying it is a good argument and we ought to pay attention to it.

MS. HUANG: Correct.

THE COURT: All right. Now I understand your position. What do you want to say? What I want to hear about is the –

MR. TILLERY: SLUSA.

THE COURT: I don't need, you know.

MR. TILLERY: Let's talk just for a moment about the SEC brief if we can. And I think you've nailed the one point that I wanted to make to this court, and that is that when they come in making an argument, a legal argument, and they're not relying upon their administrative judgment or decision making they're entitled to no more deference than anybody else who makes you a legal argument.

Here's the problem though, the cases that have interpreted the 34 Act in the in-connection-with language all of that has been now – let's see how many years, 30 years or so – there's been a body of law developed regarding the in-connection-with language. SLUSA comes along and Congress [26] adopts precisely the same language. There is yet another body of law, at least a discussion that appears throughout cases, that when Congress knows the interpretation of specific statutory language and decides to use that precise language in related legislation that they don't mean some other distinct meaning for that legislation. That in-connection-with would be interpreted the same way. There is nothing. You scour through SLUSA, look through any of these acts, you will find no basis to conclude that Congress meant the interpretation that the SEC is now trying to apply. That in-connection-with should be interpreted differently.

And here a holder status is clearly outside the scope of SLUSA. It should – it clearly are not within the scope of that act and the case should be remanded. I think there's no difference here in the analysis, your Honor, related to what the cases that you've seen and the analysis that's been undertaken in other related cases over the last six or seven months.

THE COURT: Anything you want to add?

MS. HUANG: I would just say, far from the SEC suggesting that the SLUSA language should be interpreted differently from the 10(b) language, I think the SEC's argument is precisely that it should be interpreted exactly as it is in the 10(b) language. And the only thing that's important is

that the plaintiff has suggested that the 10(b) language [27] in-connection-with is the *Blue Chips* language. But *Blue Chips* is a completely separate standard argument which has nothing to do how to appropriately interpret the in-connection-with language and the SEC says interpret it exactly as it is interpreted in 10(b).

That interpretation tells you as long as somebody held in reliance on research reports in connection with its brokage [*sic*] account that is sufficiently reasonably calculated to affect in the vesting public that that qualifies under the in-connection language. That is the SEC argument: Follow the law of 10(b).

THE COURT: I disagree. I remand. Here's my thinking: The bankruptcy in-connection-with issue is fairly easy and doesn't require much comment. What we have here is an inchoate claim which would never be sufficient for federal court jurisdiction.

The diversity issue, the amount in controversy argument, is well made. When I say "well made" I don't mean that it's valid. I mean that it's just the best argument that can be made. The attorneys' fees issue is out under *Gardynski*. And in so far as the common-fund theory is concerned there's no imaginable circumstances that the court could ever take this fund and attribute to any one plaintiff. It just couldn't happen. So you do get back to the argument here of federal question jurisdiction.

Well, our court in the Seventh Circuit has followed [28] *Merrell Dow* consistently. So just a substantial federal question will never get you federal jurisdiction except in those instances where the federal statute or federal regulation that is a necessary part of the claim also provides for a remedy, and we don't have that there. So we get to the reform act.

Now the plaintiff in this case went to great pains to say: I'm a holder. In the end it comes down to a question of statutory interpretation in this instance. Now in this instance where the question is: Is there federal subject matter jurisdiction? I construe the statute narrowly. I have

no literary license at all. And the statute talks about in connection with a sale or purchase. I would have to say that the statute here in the Securities Reform Act – SLUSA I guess is the way you say it – doesn't really say what Congress meant it to say, and I'm not at liberty to do that. The court jealously guards its subject matter jurisdiction.

There is not subject matter jurisdiction here. I will enter just a short order for the reasons I've stated here on the record remanding the case for lack of subject matter jurisdiction. I say no more than that. Thank you for your arguments.

MS. HUANG: Your Honor, may I make a motion?

THE COURT: What motion do you wish to make?

MS. HUANG: I would like to make a motion for the stay [29] of effectiveness of the court's remand order pending appeal pursuant to the 1291 because as you know under *Kircher* an appeal is available because this is a final decision under the court's Seventh Circuit recent precedent.

THE COURT: Now Judge Herndon's case. Do you want to talk about that, the one that's up there now?

MS. HUANG: *Kircher* which is still on appeal before the Seventh Circuit.

THE COURT: But in that case as I understand it Judge Easterbrook's opinion he said the judge didn't just remand the case for want of subject matter jurisdiction, he did more. Isn't that right?

MR. TILLERY: That's correct.

THE COURT: I'm not – I'm specifically saying I'm not getting to the merits of anything.

MS. HUANG: With apologies, your Honor. It is my understanding that the finding of the court in the *Kircher* case that by its nature SLUSA provides for removal and there is subject matter jurisdiction for the court then to determine whether or not remand is appropriate under SLUSA, which I believe is the effect of this court's order. I

would also refer the court to the recent *Woodbury* decision order issued by Judge Reagan, I believe it is, issued a couple of weeks ago granting a stay in that case for an appeal pending – for a stay of those proceedings pending the resolution of the *Kircher* [30] appeal.

THE COURT: I will read *Kircher*, but – do you want to –

MR. TILLERY: First of all, I would like an opportunity to respond rather than an oral motion for stay. I don't know that it is even appropriate, first of all.

THE COURT: The first thing. What I will do is I will read the opinion again in *Kircher*, all right. Now if I – if I'm right on this – and I want to read *Kircher* again it's been about a week or so and these cases tend to dance around – I don't have – you can't stay a case over which you don't have jurisdiction.

MR. TILLERY: That's correct.

THE COURT: On the other hand, if you're right and there is an exception here I will consider it. I'll get to you shortly.

MR. TILLERY: The only thing I want to point out is – I think you just hit it – how does this court enter a stay if it's decided –

THE COURT: I can't. But I want to read *Kircher* again. I will read it.

MS. HUANG: We will be happy to submit in writing –

THE COURT: I'll read it.

MS. HUANG: – a one-page letter. We promise we won't go over that.

[31] THE COURT: I'll tell what, you need to get to it me before noon today. So if you can get over there and start – if Mr. Whyte's office has computers and you can send me one I'll read it, but I'm going to read the opinion and do it. But I mean, that's all I'm going to do is read the opinion.

MR. TILLERY: Well, I mean, fundamentally it comes down to if they believe they have appeal rights your deci-

sion of no jurisdiction in this matter that somehow doesn't reinvest within this court the authority to grant a stay.

THE COURT: I agree with you.

MR. TILLERY: All right.

THE COURT: Court's in recess. I'll get something out today.

(End of requested transcript)

[Reporter's Certificate Omitted]

STATUTORY AND REGULATORY PROVISIONS INVOLVED

15 U.S.C. § 77p provides:

§ 77p. Additional remedies; limitation on remedies

(a) Remedies additional

Except as provided in subsection (b) of this section, the rights and remedies provided by this subchapter shall be in addition to any and all other rights and remedies that may exist at law or in equity.

(b) Class action limitations

No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging –

(1) an untrue statement or omission of a material fact in connection with the purchase or sale of a covered security; or

(2) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.

(c) Removal of covered class actions

Any covered class action brought in any State court involving a covered security, as set forth in subsection (b) of this section, shall be removable to the Federal district court for the district in which the action is pending, and shall be subject to subsection (b) of this section.

(d) Preservation of certain actions

(1) Actions under State law of State of incorporation

(A) Actions preserved

Notwithstanding subsection (b) or (c) of this section, a covered class action described in subparagraph (B) of this paragraph that is based upon the statutory or common law of the State in which the issuer is incorporated (in the case of a corporation) or organized (in the case of any other entity) may be maintained in a State or Federal court by a private party.

(B) Permissible actions

A covered class action is described in this subparagraph if it involves –

(i) the purchase or sale of securities by the issuer or an affiliate of the issuer exclusively from or to holders of equity securities of the issuer; or

(ii) any recommendation, position, or other communication with respect to the sale of securities of the issuer that –

(I) is made by or on behalf of the issuer or an affiliate of the issuer to holders of equity securities of the issuer; and

(II) concerns decisions of those equity holders with respect to voting their securities, acting in response to a tender or exchange offer, or exercising dissenters' or appraisal rights.

(2) State actions

(A) In general

Notwithstanding any other provision of this section, nothing in this section may be construed to preclude a State or political subdivision thereof or a State pension plan from bringing an action involving

a covered security on its own behalf, or as a member of a class comprised solely of other States, political subdivisions, or State pension plans that are named plaintiffs, and that have authorized participation, in such action.

(B) "State pension plan" defined

For purposes of this paragraph, the term "State pension plan" means a pension plan established and maintained for its employees by the government of the State or political subdivision thereof, or by any agency or instrumentality thereof.

(3) Actions under contractual agreements between issuers and indenture trustees

Notwithstanding subsection (b) or (c) of this section, a covered class action that seeks to enforce a contractual agreement between an issuer and an indenture trustee may be maintained in a State or Federal court by a party to the agreement or a successor to such party.

(4) Remand of removed actions

In an action that has been removed from a State court pursuant to subsection (c) of this section, if the Federal court determines that the action may be maintained in State court pursuant to this subsection, the Federal court shall remand such action to such State court.

(e) Preservation of State jurisdiction

The securities commission (or any agency or office performing like functions) of any State shall retain jurisdiction under the laws of such State to investigate and bring enforcement actions.

(f) Definitions

For purposes of this section, the following definitions shall apply:

(1) Affiliate of the issuer

The term "affiliate of the issuer" means a person that directly or indirectly, through one or more intermediaries, controls or is controlled by or is under common control with, the issuer.

(2) Covered class action

(A) In general

The term "covered class action" means –

(i) any single lawsuit in which –

(I) damages are sought on behalf of more than 50 persons or prospective class members, and questions of law or fact common to those persons or members of the prospective class, without reference to issues of individualized reliance on an alleged misstatement or omission, predominate over any questions affecting only individual persons or members; or

(II) one or more named parties seek to recover damages on a representative basis on behalf of themselves and other unnamed parties similarly situated, and questions of law or fact common to those persons or members of the prospective class predominate over any questions affecting only individual persons or members; or

(ii) any group of lawsuits filed in or pending in the same court and involving common questions of law or fact, in which –

(I) damages are sought on behalf of more than 50 persons; and

(II) the lawsuits are joined, consolidated, or otherwise proceed as a single action for any purpose.

(B) Exception for derivative actions

Notwithstanding subparagraph (A), the term "covered class action" does not include an exclusively derivative action brought by one or more shareholders on behalf of a corporation.

(C) Counting of certain class members

For purposes of this paragraph, a corporation, investment company, pension plan, partnership, or other entity, shall be treated as one person or prospective class member, but only if the entity is not established for the purpose of participating in the action.

(D) Rule of construction

Nothing in this paragraph shall be construed to affect the discretion of a State court in determining whether actions filed in such court should be joined, consolidated, or otherwise allowed to proceed as a single action.

(3) Covered security

The term "covered security" means a security that satisfies the standards for a covered security specified in paragraph (1) or (2) of section 77r(b) of this title at the time during which it is alleged that the misrepresentation, omission, or manipulative or deceptive conduct occurred, except that such term shall not include any debt security that is exempt from registration under this subchapter pursuant to rules issued by the Commission under section 77d(2) of this title.

15 U.S.C. § 78j provides:

§ 78j. Manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange –

(a)(1) To effect a short sale, or to use or employ any stop-loss order in connection with the purchase or sale, of any security registered on a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(2) Paragraph (1) of this subsection shall not apply to security futures products.

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement (as defined in section 206B of the Gramm-Leach-Bliley Act), any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Rules promulgated under subsection (b) of this section that prohibit fraud, manipulation, or insider trading (but not rules imposing or specifying reporting or recordkeeping requirements, procedures, or standards as prophylactic measures against fraud, manipulation, or insider trading), and judicial precedents decided under subsection (b) of this section and rules promulgated thereunder that prohibit fraud, manipulation, or insider trading, shall apply to security-based swap agreements (as defined in section 206B of the Gramm-Leach-Bliley Act) to the same extent as they apply to securities. Judicial precedents decided under section 77q(a) of this title and sections 78i,

78o, 78p, 78t, and 78u-1 of this title, and judicial precedents decided under applicable rules promulgated under such sections, shall apply to security-based swap agreements (as defined in section 206B of the Gramm-Leach-Bliley Act) to the same extent as they apply to securities.

15 U.S.C. § 78bb provides:

§ 78bb. Effect on existing law

(a) Addition of rights and remedies; recovery of actual damages; State securities commissions

Except as provided in subsection (f) of this section, the rights and remedies provided by this chapter shall be in addition to any and all other rights and remedies that may exist at law or in equity; but no person permitted to maintain a suit for damages under the provisions of this chapter shall recover, through satisfaction of judgment in one or more actions, a total amount in excess of his actual damages on account of the act complained of. Except as otherwise specifically provided in this chapter, nothing in this chapter shall affect the jurisdiction of the securities commission (or any agency or officer performing like functions) of any State over any security or any person insofar as it does not conflict with the provisions of this chapter or the rules and regulations thereunder. No State law which prohibits or regulates the making or promoting of wagering or gaming contracts, or the operation of "bucket shops" or other similar or related activities, shall invalidate any put, call, straddle, option, privilege, or other security subject to this chapter, or apply to any activity which is incidental or related to the offer, purchase, sale, exercise, settlement, or closeout of any such security. No provision of State law regarding the offer, sale, or distribution of securities shall apply to any transaction in a security futures product, except that this sentence shall not be construed as limiting any State antifraud law of general applicability.

(b) Modification of disciplinary procedures

Nothing in this chapter shall be construed to modify existing law with regard to the binding effect (1) on any member of or participant in any self-regulatory organization of any action taken by the authorities of such organization to settle disputes between its members or partici-

pants, (2) on any municipal securities dealer or municipal securities broker of any action taken pursuant to a procedure established by the Municipal Securities Rulemaking Board to settle disputes between municipal securities dealers and municipal securities brokers, or (3) of any action described in paragraph (1) or (2) on any person who has agreed to be bound thereby.

(c) Continuing validity of disciplinary sanctions

The stay, setting aside, or modification pursuant to section 78s(e) of this title of any disciplinary sanction imposed by a self-regulatory organization on a member thereof, person associated with a member, or participant therein, shall not affect the validity or force of any action taken as a result of such sanction by the self-regulatory organization prior to such stay, setting aside, or modification: *Provided*, That such action is not inconsistent with the provisions of this chapter or the rules or regulations thereunder. The rights of any person acting in good faith which arise out of any such action shall not be affected in any way by such stay, setting aside, or modification.

(d) Physical location of facilities of registered clearing agencies or registered transfer agents not to subject changes in beneficial or record ownership of securities to State or local taxes

No State or political subdivision thereof shall impose any tax on any change in beneficial or record ownership of securities effected through the facilities of a registered clearing agency or registered transfer agent or any nominee thereof or custodian therefor or upon the delivery or transfer of securities to or through or receipt from such agency or agent or any nominee thereof or custodian therefor, unless such change in beneficial or record ownership or such transfer or delivery or receipt would otherwise be taxable by such State or political subdivision if the facilities of such registered clearing agency, registered transfer agent, or any nominee thereof or custodian therefor were not physically located in the taxing State or

political subdivision. No State or political subdivision thereof shall impose any tax on securities which are deposited in or retained by a registered clearing agency, registered transfer agent, or any nominee thereof or custodian therefor, unless such securities would otherwise be taxable by such State or political subdivision if the facilities of such registered clearing agency, registered transfer agent, or any nominee thereof or custodian therefor were not physically located in the taxing State or political subdivision.

(e) Exchange, broker, and dealer commissions; brokerage and research services

(1) No person using the mails, or any means or instrumentality of interstate commerce, in the exercise of investment discretion with respect to an account shall be deemed to have acted unlawfully or to have breached a fiduciary duty under State or Federal law unless expressly provided to the contrary by a law enacted by the Congress or any State subsequent to June 4, 1975, solely by reason of his having caused the account to pay a member of an exchange, broker, or dealer an amount of commission for effecting a securities transaction in excess of the amount of commission another member of an exchange, broker, or dealer would have charged for effecting that transaction, if such person determined in good faith that such amount of commission was reasonable in relation to the value of the brokerage and research services provided by such member, broker, or dealer, viewed in terms of either that particular transaction or his overall responsibilities with respect to the accounts as to which he exercises investment discretion. This subsection is exclusive and plenary insofar as conduct is covered by the foregoing, unless otherwise expressly provided by contract: *Provided*, however, That nothing in this subsection shall be construed to impair or limit the power of the Commission under any other provision of this chapter or otherwise.

(2) A person exercising investment discretion with respect to an account shall make such disclosure of his policies and practices with respect to commissions that will be paid for effecting securities transactions, at such times and in such manner, as the appropriate regulatory agency, by rule, may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(3) For purposes of this subsection a person provides brokerage and research services insofar as he –

(A) furnishes advice, either directly or through publications or writings, as to the value of securities, the advisability of investing in, purchasing, or selling securities, and the availability of securities or purchasers or sellers of securities;

(B) furnishes analyses and reports concerning issuers, industries, securities, economic factors and trends, portfolio strategy, and the performance of accounts; or

(C) effects securities transactions and performs functions incidental thereto (such as clearance, settlement, and custody) or required in connection therewith by rules of the Commission or a self-regulatory organization of which such person is a member or person associated with a member or in which such person is a participant.

(4) The provisions of this subsection shall not apply with regard to securities that are security futures products.

(f) Limitations on remedies

(1) Class action limitations

No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging –

(A) a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security; or

(B) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.

(2) Removal of covered class actions

Any covered class action brought in any State court involving a covered security, as set forth in paragraph (1), shall be removable to the Federal district court for the district in which the action is pending, and shall be subject to paragraph (1).

(3) Preservation of certain actions

(A) Actions under State law of State of incorporation

(i) Actions preserved

Notwithstanding paragraph (1) or (2), a covered class action described in clause (ii) of this subparagraph that is based upon the statutory or common law of the State in which the issuer is incorporated (in the case of a corporation) or organized (in the case of any other entity) may be maintained in a State or Federal court by a private party.

(ii) Permissible actions

A covered class action is described in this clause if it involves –

(I) the purchase or sale of securities by the issuer or an affiliate of the issuer exclusively from or to holders of equity securities of the issuer; or

(II) any recommendation, position, or other communication with respect to the sale of securities of an issuer that –

(aa) is made by or on behalf of the issuer or an affiliate of the issuer to holders of equity securities of the issuer; and

(bb) concerns decisions of such equity holders with respect to voting their securities, acting in response to a tender or exchange offer, or exercising dissenters' or appraisal rights.

(B) State actions

(i) In general

Notwithstanding any other provision of this subsection, nothing in this subsection may be construed to preclude a State or political subdivision thereof or a State pension plan from bringing an action involving a covered security on its own behalf, or as a member of a class comprised solely of other States, political subdivisions, or State pension plans that are named plaintiffs, and that have authorized participation, in such action.

(ii) State pension plan defined

For purposes of this subparagraph, the term "State pension plan" means a pension plan established and maintained for its employees by the government of a State or political subdivision thereof, or by any agency or instrumentality thereof.

(C) Actions under contractual agreements between issuers and indenture trustees

Notwithstanding paragraph (1) or (2), a covered class action that seeks to enforce a contractual agreement between an issuer and an indenture trustee may be maintained in a State or Federal court by a party to the agreement or a successor to such party.

(D) Remand of removed actions

In an action that has been removed from a State court pursuant to paragraph (2), if the Federal court determines that the action may be maintained in State court pursuant to this subsection, the Federal court shall remand such action to such State court.

(4) Preservation of State jurisdiction

The securities commission (or any agency or office performing like functions) of any State shall retain jurisdiction under the laws of such State to investigate and bring enforcement actions.

(5) Definitions

For purposes of this subsection, the following definitions shall apply:

(A) Affiliate of the issuer

The term "affiliate of the issuer" means a person that directly or indirectly, through one or more intermediaries, controls or is controlled by or is under common control with, the issuer.

(B) Covered class action

The term "covered class action" means –

(i) any single lawsuit in which –

(I) damages are sought on behalf of more than 50 persons or prospective class members, and questions of law or fact common to those persons or members of the prospective class, without reference to issues of individualized reliance on an alleged misstatement or omission, predominate over any questions affecting only individual persons or members; or

(II) one or more named parties seek to recover damages on a representative basis on behalf of themselves and other unnamed parties

similarly situated, and questions of law or fact common to those persons or members of the prospective class predominate over any questions affecting only individual persons or members; or

(ii) any group of lawsuits filed in or pending in the same court and involving common questions of law or fact, in which –

(I) damages are sought on behalf of more than 50 persons; and

(II) the lawsuits are joined, consolidated, or otherwise proceed as a single action for any purpose.

(C) Exception for derivative actions

Notwithstanding subparagraph (B), the term "covered class action" does not include an exclusively derivative action brought by one or more shareholders on behalf of a corporation.

(D) Counting of certain class members

For purposes of this paragraph, a corporation, investment company, pension plan, partnership, or other entity, shall be treated as one person or prospective class member, but only if the entity is not established for the purpose of participating in the action.

(E) Covered security

The term "covered security" means a security that satisfies the standards for a covered security specified in paragraph (1) or (2) of section 18(b) of the Securities Act of 1933 [15 U.S.C. 77r(b)], at the time during which it is alleged that the misrepresentation, omission, or manipulative or deceptive conduct occurred, except that such term shall not include any debt security that is exempt from registration under the Securities Act of 1933 [15 U.S.C. 77a et seq.] pursuant to

rules issued by the Commission under section 4(2) of that Act [15 U.S.C. 77d(2)].

(F) Rule of construction

Nothing in this paragraph shall be construed to affect the discretion of a State court in determining whether actions filed in such court should be joined, consolidated, or otherwise allowed to proceed as a single action.

28 U.S.C. § 1291 provides:

§ 1291. Final decisions of district courts

The courts of appeals (other than the United States Court of Appeals for the Federal Circuit) shall have jurisdiction of appeals from all final decisions of the district courts of the United States, the United States District Court for the District of the Canal Zone, the District Court of Guam, and the District Court of the Virgin Islands, except where a direct review may be had in the Supreme Court. The jurisdiction of the United States Court of Appeals for the Federal Circuit shall be limited to the jurisdiction described in sections 1292(c) and (d) and 1295 of this title.

28 U.S.C. § 1331 provides:

§ 1331. Federal question

The district courts shall have original jurisdiction of all civil actions arising under the Constitution, laws, or treaties of the United States.

28 U.S.C. § 1332 provides:

§ 1332. Diversity of citizenship; amount in controversy; costs

(a) The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of $75,000, exclusive of interest and costs, and is between –

(1) citizens of different States;

(2) citizens of a State and citizens or subjects of a foreign state;

(3) citizens of different States and in which citizens or subjects of a foreign state are additional parties; and

(4) a foreign state, defined in section 1603(a) of this title, as plaintiff and citizens of a State or of different States.

For the purposes of this section, section 1335, and section 1441, an alien admitted to the United States for permanent residence shall be deemed a citizen of the State in which such alien is domiciled.

(b) Except when express provision therefor is otherwise made in a statute of the United States, where the plaintiff who files the case originally in the Federal courts is finally adjudged to be entitled to recover less than the sum or value of $75,000, computed without regard to any setoff or counterclaim to which the defendant may be adjudged to be entitled, and exclusive of interest and costs, the district court may deny costs to the plaintiff and, in addition, may impose costs on the plaintiff.

(c) For the purposes of this section and section 1441 of this title –

(1) a corporation shall be deemed to be a citizen of any State by which it has been incorporated and of the State where it has its principal place of business, except that in any direct action against the insurer of a policy or

contract of liability insurance, whether incorporated or unincorporated, to which action the insured is not joined as a party-defendant, such insurer shall be deemed a citizen of the State of which the insured is a citizen, as well as of any State by which the insurer has been incorporated and of the State where it has its principal place of business; and

(2) the legal representative of the estate of a decedent shall be deemed to be a citizen only of the same State as the decedent, and the legal representative of an infant or incompetent shall be deemed to be a citizen only of the same State as the infant or incompetent.

(d) The word "States", as used in this section, includes the Territories, the District of Columbia, and the Commonwealth of Puerto Rico.

28 U.S.C. § 1441 provides:

§ 1441. Actions removable generally

(a) Except as otherwise expressly provided by Act of Congress, any civil action brought in a State court of which the district courts of the United States have original jurisdiction, may be removed by the defendant or the defendants, to the district court of the United States for the district and division embracing the place where such action is pending. For purposes of removal under this chapter, the citizenship of defendants sued under fictitious names shall be disregarded.

(b) Any civil action of which the district courts have original jurisdiction founded on a claim or right arising under the Constitution, treaties or laws of the United States shall be removable without regard to the citizenship or residence of the parties. Any other such action shall be removable only if none of the parties in interest properly joined and served as defendants is a citizen of the State in which such action is brought.

(c) Whenever a separate and independent claim or cause of action within the jurisdiction conferred by section 1331 of this title is joined with one or more otherwise nonremovable claims or causes of action, the entire case may be removed and the district court may determine all issues therein, or, in its discretion, may remand all matters in which State law predominates.

(d) Any civil action brought in a State court against a foreign state as defined in section 1603(a) of this title may be removed by the foreign state to the district court of the United States for the district and division embracing the place where such action is pending. Upon removal the action shall be tried by the court without jury. Where removal is based upon this subsection, the time limitations of section 1446(b) of this chapter may be enlarged at any time for cause shown.

(e)(1) Notwithstanding the provisions of subsection (b) of this section, a defendant in a civil action in a State court may remove the action to the district court of the United States for the district and division embracing the place where the action is pending if –

(A) the action could have been brought in a United States district court under section 1369 of this title; or

(B) the defendant is a party to an action which is or could have been brought, in whole or in part, under section 1369 in a United States district court and arises from the same accident as the action in State court, even if the action to be removed could not have been brought in a district court as an original matter.

The removal of an action under this subsection shall be made in accordance with section 1446 of this title, except that a notice of removal may also be filed before trial of the action in State court within 30 days after the date on which the defendant first becomes a party to an action under section 1369 in a United States district court that arises from the same accident as the action in State court, or at a later time with leave of the district court.

(2) Whenever an action is removed under this subsection and the district court to which it is removed or transferred under section 1407(j) has made a liability determination requiring further proceedings as to damages, the district court shall remand the action to the State court from which it had been removed for the determination of damages, unless the court finds that, for the convenience of parties and witnesses and in the interest of justice, the action should be retained for the determination of damages.

(3) Any remand under paragraph (2) shall not be effective until 60 days after the district court has issued an order determining liability and has certified its intention to remand the removed action for the determination of damages. An appeal with respect to the liability determi-

nation of the district court may be taken during that 60-day period to the court of appeals with appellate jurisdiction over the district court. In the event a party files such an appeal, the remand shall not be effective until the appeal has been finally disposed of. Once the remand has become effective, the liability determination shall not be subject to further review by appeal or otherwise.

(4) Any decision under this subsection concerning remand for the determination of damages shall not be reviewable by appeal or otherwise.

(5) An action removed under this subsection shall be deemed to be an action under section 1369 and an action in which jurisdiction is based on section 1369 of this title for purposes of this section and sections 1407, 1697, and 1785 of this title.

(6) Nothing in this subsection shall restrict the authority of the district court to transfer or dismiss an action on the ground of inconvenient forum.

(f) The court to which a civil action is removed under this section is not precluded from hearing and determining any claim in such civil action because the State court from which such civil action is removed did not have jurisdiction over that claim.

28 U.S.C. § 1447 provides:

§ 1447. Procedure after removal generally

(a) In any case removed from a State court, the district court may issue all necessary orders and process to bring before it all proper parties whether served by process issued by the State court or otherwise.

(b) It may require the removing party to file with its clerk copies of all records and proceedings in such State court or may cause the same to be brought before it by writ of certiorari issued to such State court.

(c) A motion to remand the case on the basis of any defect other than lack of subject matter jurisdiction must be made within 30 days after the filing of the notice of removal under section 1446(a). If at any time before final judgment it appears that the district court lacks subject matter jurisdiction, the case shall be remanded. An order remanding the case may require payment of just costs and any actual expenses, including attorney fees, incurred as a result of the removal. A certified copy of the order of remand shall be mailed by the clerk to the clerk of the State court. The State court may thereupon proceed with such case.

(d) An order remanding a case to the State court from which it was removed is not reviewable on appeal or otherwise, except that an order remanding a case to the State court from which it was removed pursuant to section 1443 of this title shall be reviewable by appeal or otherwise.

(e) If after removal the plaintiff seeks to join additional defendants whose joinder would destroy subject matter jurisdiction, the court may deny joinder, or permit joinder and remand the action to the State court.

17 C.F.R. § 240.10b-5 provides:

§ 240.10b-5. Employment of manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

Supreme Court of the United States

Office of the Clerk
Washington, DC 20543-0001

WILLIAM K. SUTER
Clerk of the Court
(202) 479-3011

November 9, 2005

Mr. David C. Frederick
Kellogg Huber Hansen
Todd, Evans & Figel, P.L.L.C.
1615 M Street, N.W.
Suite 400
Washington, DC 20036

Re: Richard Disher
v. Citigroup Global Markets Incorporated
Application No. 05A409

Dear Mr. Frederick:

The application for an extension of time within which to file a petition for a writ of certiorari in the above-entitled case has been presented to Justice Stevens, who on November 9, 2005 extended the time to and including December 15, 2005.

This letter has been sent to those designated on the attached notification list.

Sincerely,

William K. Suter, Clerk
by
/s/ MELISSA BLALOCK
Melissa Blalock
Case Analyst

[attached notification list omitted]

FILED
FEB 16 2006
OFFICE OF THE CLERK
SUPREME COURT, U.S.

No. 05-776

IN THE

Supreme Court of the United States

RICHARD DISHER, INDIVIDUALLY AND
ON BEHALF OF ALL OTHERS SIMILARLY SITUATED,

Petitioner,

v.

CITIGROUP GLOBAL MARKETS INC.,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

RESPONDENT'S BRIEF IN OPPOSITION

RICHARD A. ROSEN
BRAD S. KARP
WALTER RIEMAN*
PAUL, WEISS, RIFKIND,
WHARTON & GARRISON LLP
1285 Avenue of the Americas
New York, New York 10019-6064
(212) 373-3000

Counsel for Respondent

**Counsel of record*

February 16, 2006

QUESTIONS PRESENTED

1. Does a federal court of appeals have jurisdiction to review a district court's order remanding to state court an action removed under the Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, 112 Stat. 3227 ("SLUSA"), where the district court remanded based on its view that the plaintiff had not alleged an untrue statement or omission of material fact "in connection with the purchase or sale" of a covered security within the meaning of the principal substantive rule set forth in SLUSA?

2. Does SLUSA prohibit private parties from maintaining state-law "holder" class actions brought on behalf of persons who assert that they were induced by allegedly fraudulent statements or omissions to hold (i.e., refrain from selling), as opposed to purchase or sell, securities?

RULE 29.6 STATEMENT

Citigroup Global Markets Inc. (formerly known as Salomon Smith Barney Inc.) is a wholly owned subsidiary of Citigroup Financial Products Inc. (formerly known as Salomon Brothers Holding Company Inc.), which is a wholly owned subsidiary of Citigroup Global Markets Holdings Inc. (formerly known as Salomon Smith Barney Holdings Inc.), which is a wholly owned subsidiary of Citigroup Inc.

Citigroup Inc. is a publicly traded corporation that has no parent corporation. No publicly held corporation owns 10% or more of its stock.

TABLE OF CONTENTS

QUESTIONS PRESENTED i

RULE 29.6 STATEMENT ii

TABLE OF AUTHORITIES v

RESPONDENT'S BRIEF IN OPPOSITION 1

STATEMENT OF THE CASE 2

A. The Statutory Framework 2

B. The Complaint 4

C. Proceedings Before the District Court 6

D. Proceedings Before the Seventh Circuit 8

REASONS FOR DENYING THE PETITION 11

I. THIS COURT SHOULD RULE IN *DABIT* THAT SLUSA BARS CLASS ACTIONS ASSERTING HOLDER CLAIMS, AND SHOULD THEREFORE DENY CERTIORARI ON QUESTION 2 11

II. THIS COURT SHOULD DENY CERTIORARI ON THE JURISDICTIONAL ISSUE PRESENTED IN QUESTION 1 14

A. This Court Should Rule in *Kircher* that a Court of Appeals May Review an Order Remanding an Action to State Court Based on the "in Connection with" Requirement 14

B. If this Court Rules in *Dabit* that SLUSA Bars Class Actions Asserting Holder Claims, the Court Should Deny Certiorari in this Case Regardless of the Outcome in *Kircher* 14

CONCLUSION 18

TABLE OF AUTHORITIES

CASES

Blue Chip Stamps v. *Manor Drug Stores*, 421 U.S. 732 (1975) 6, 10

Crocker v. *FDIC*, 826 F.2d 347 (5th Cir. 1987) 12

Holmes v. *Investor Prot. Corp.*, 503 U.S. 258 (1992) 7

Kircher v. *Putnam Funds Trust*, 373 F.3d 847 (7th Cir. 2004), *cert. granted*, 126 S. Ct. 979 (2005) ..... *passim*

Kircher v. *Putnam Funds Trust*, 403 F.3d 478 (7th Cir. 2005), *cert. granted*, 126 S. Ct. 979 (2005) 10

Lawrence v. *Chater*, 516 U.S. 163 (1996) (per curiam) 16, 17

Rowinski v. *Salomon Smith Barney Inc.*, 398 F.3d 294 (3d Cir. 2005) 13

SEC v. *Zandford*, 535 U.S. 813 (2002) 7, 11

Thermtron Prods., Inc. v. *Hermansdorfer*, 423 U.S. 336 (1976) 9

Things Remembered, Inc. v. *Petrarca*, 516 U.S. 124 (1995) 9

STATUTES AND REGULATIONS

Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 2

Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, § 2(1)-(3), (5) 112 Stat. 3227, 3227 2

Securities Act of 1933, 15 U.S.C. §§ 77a *et seq.* 1, 3, 4, 6, 14

15 U.S.C. § 77p(b) 1, 3, 6, 14

15 U.S.C. § 77p(c) 3, 4, 6

Securities Exchange Act of 1934, 15 U.S.C. §§ 78a *et seq.* 1, 2, 3, 4, 6, 14

15 U.S.C. § 78u-4(b), 78u-5 2

15 U.S.C. § 78j(b)(§ 10(b)) 6

15 U.S.C. § 78bb(f)(1) 1, 3, 6, 14

15 U.S.C. § 78bb(f)(2) 3, 4, 6

17 C.F.R. § 240.10b-5 (Rule 10b-5) 6

LEGISLATIVE MATERIALS

H.R. Rep. No. 105-640 (1998) 3

RESPONDENT'S BRIEF IN OPPOSITION

The petition in this case presents two questions, one substantive and one procedural, each of which is also presented by another case in which this Court has previously granted certiorari. The substantive question, Question 2 in the petition, concerns whether SLUSA bars certain class actions brought by holders (as distinct from purchasers and sellers) of securities. That question is before the Court in *Merrill Lynch, Pierce, Fenner & Smith Inc.* v. *Dabit*, No. 04-1371 (argued Jan. 18, 2006). The procedural question, Question 1 in the petition, concerns whether a court of appeals may review a district court's order remanding an action to state court under SLUSA on particular grounds. That question is before the Court in *Kircher* v. *Putnam Funds Trust*, No. 05-409 (certiorari granted Jan. 6, 2006). Plenary review by the Court of the questions presented in the petition in this case will therefore not be necessary; both of those questions will be decided in other cases.

In the view of respondent Citigroup Global Markets Inc. ("Citigroup"), the Court should decide the questions presented in *Dabit* and *Kircher* in accordance with the Seventh Circuit's decision in this case. In other words, the Court should reverse the Second Circuit's ruling in *Dabit*, and hold that SLUSA bars class actions by holders of securities that otherwise fall within SLUSA's prohibition on the maintenance of certain class actions brought under state law. In *Kircher*, the Court should hold that a court of appeals may review a district court's order remanding a class action under SLUSA based on the district court's finding that the action does not allege misrepresentations, omissions, or manipulations "in connection with the purchase or sale" of a covered security. 15 U.S.C. §§ 77p(b), 78bb(f)(1).

Citigroup also respectfully submits that the petition in this case should be held pending this Court's plenary decision in *Dabit* of the substantive question. If the *Dabit* Court agrees with the position of Citigroup, and of the Seventh Circuit in the opinion below, on the issue presented in *Dabit*, the Court should deny certiorari in this case, regardless of the outcome of the procedural issue in *Kircher*. If Citigroup is correct on the *Dabit* issue, it necessarily follows that petitioner's class action was properly dismissed. As Citigroup further explains below, if Citigroup's view prevails in *Dabit*, no outcome in *Kircher* could change the proper ultimate result in this case — i.e., dismissal of petitioner's putative class action — or could warrant a grant of certiorari, vacatur of the judgment below, and remand in light of the Court's decision in *Kircher*.

STATEMENT OF THE CASE

A. The Statutory Framework

As petitioner acknowledges, Congress enacted SLUSA in order to prevent plaintiffs in class actions from evading the requirements of the Private Securities Litigation Reform Act of 1995 (the "PSLRA"), Pub. L. No. 104-67, 109 Stat. 737. *See* Pet. 5. The PSLRA adopted reforms applicable to private actions brought under the Securities Exchange Act of 1934, such as a safe harbor for forward-looking statements, heightened pleading standards, an automatic stay of discovery, and provisions governing the appointment of lead plaintiffs and counsel in class actions. *See* 15 U.S.C. § 78u-4(b), 78u-5. Congress, however, subsequently determined that plaintiffs were "prevent[ing] [the PSLRA] from fully achieving its objectives" by bringing securities-related class actions in state courts based on state law. SLUSA § 2(1)-(3), (5), 112 Stat. 3227, 3227 (1998).

Congress consequently enacted SLUSA, which prohibits the maintenance in federal or state court of certain state-law class actions involving securities. The relevant substantive prohibition in SLUSA is as follows:

> No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging —
>
> > (1) an untrue statement or omission of a material fact in connection with the purchase or sale of a covered security; or
> >
> > (2) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.

15 U.S.C. § 77p(b); *accord id.* § 78bb(f)(1).

Congress, which was concerned that state courts might not properly apply this prohibition (*see* H.R. Rep. No. 105-640, at 16 (1998)), also provided in SLUSA for the removal from state court to federal court of a broader category of state-law class actions, so that a federal district court could decide whether SLUSA's substantive prohibition bars the particular class action. The relevant provision governing removal, which immediately follows the passage quoted above, is as follows:

> Any covered class action brought in any State court involving a covered security, as set forth in subsection (b), shall be removable to the Federal district court for the district in which the action is pending, and shall be subject to subsection (b).

15 U.S.C. § 77p(c); *accord id.* § 78bb(f)(2). Subsection (b), as used in this passage, refers to the subsection that is set forth in the immediately preceding quotation.

B. The Complaint

Petitioner Richard Disher, acting as the putative representative plaintiff, filed a class-action complaint against Citigroup in the Circuit Court for the Third Judicial Circuit, Madison County, Illinois, on March 22, 2004. Citigroup is a full-service securities firm. *See* Pet. App. 15a, 16a-17a (¶¶ 1, 10).

As the complaint alleges, equity research analysts employed by Citigroup issue reports on the common stock of selected publicly traded companies. Those research reports assigned ratings of "buy," "outperform," "neutral," "underperform," and "sell" to common stocks. *Id.* at 17a (¶ 13). Citigroup provided this research to, among others, its retail brokerage customers. *Id.* (¶ 11). In 1998 and 1999, petitioner, who was a Citigroup brokerage customer, allegedly purchased shares of MCI WorldCom, Inc. and Rhythms NetConnections, Inc. At that time, Citigroup research analysts reported on and rated those stocks. *Id.* at 16a (¶¶ 6, 7).

According to petitioner's complaint, Citigroup's research reports and ratings on the common stocks of companies in the internet and telecommunications sectors were biased during the putative class period. *See id.* at 20a-21a (¶¶ 31-38). Citigroup allegedly "used [its] research reports, ratings and recommendations to attract new investment banking clients and to retain current investment banking clients by agreeing to issue a research rating for an investment banking client's stock more favorably than [Citigroup's] research warranted." *Id.* at 20a (¶ 34). Citigroup, petitioner charged, "secretly abandoned its

published five-point rating system and instead utilized a *de facto* three-point system ('buy,' 'outperform' and 'neutral')" (*id.* at 19a (¶ 26)), in order to "continue to rate stocks as 'buy,' 'outperform' or 'neutral,' even after Citigroup's analysts no longer believed that such ratings were warranted for particular [stocks in the internet and telecommunications sectors] under the five-point rating system" (*id.* at 20a (¶ 32)). According to petitioner, "[b]y continuing to rate [stocks in the internet and telecommunications sectors] 'buy,' 'outperform' or 'neutral' under the secret three-point rating system, [Citigroup] induced its customers to continue holding those securities . . . ." *Id.* at 20a (¶ 33).

Petitioner brought his action on behalf of a putative class of Citigroup customers who held stocks issued by unspecified internet or telecommunications companies that were covered by Citigroup's research analysts. *Id.* at 22a (¶ 39). Such customers, the complaint stated, were members of the putative class if they held such stocks in their Citigroup accounts at times when those stocks were declining in value, and when Citigroup continued to provide positive, and allegedly unwarranted, ratings on the stocks. *Id.* The complaint asserts five common-law causes of action against Citigroup, all of which are based on state law, and all of which depend on petitioner's allegation that putative class members held securities in reliance on Citigroup's supposedly biased research and ratings.[1] The complaint purports to exclude "any claims based upon [Citigroup's] conduct in connection with [petitioner's] or any Class member's purchases or sales" of the securities at issue. *Id.* (¶ 41).

---

[1] The complaint purports to assert claims for breach of contract, breach of fiduciary duty, fraudulent misrepresentation, unjust enrichment, and negligence. Pet. App. 25a-37a (¶¶ 51-94).